S. Hrg. 104–252

REINVENTION OF HUD AND REDIRECTION OF HOUSING POLICY

HEARINGS

BEFORE THE

SUBCOMMITTEE ON HOUSING OPPORTUNITY AND COMMUNITY DEVELOPMENT

AND THE

SUBCOMMITTEE ON HUD OVERSIGHT AND STRUCTURE

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

ON

THE MISSION, MANAGEMENT, AND PROGRAMS OF HUD AND TO EXPLORE THE VARIOUS PROPOSALS TO RESTRUCTURE OR THE POSSIBILITY TO ELIMINATE THE AGENCY IN ORDER TO IMPROVE THE DELIVERY OF HOUSING SERVICES TO AMERICAN FAMILIES AND REVITALIZE OUR NEIGHBORHOODS

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WITNESSES

REINVENTION OF HUD AND REDIRECTION OF HOUSING POLICY

TUESDAY, MARCH 14, 1995

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING OPPORTUNITY AND COMMUNITY DEVELOPMENT, AND
SUBCOMMITTEE ON HUD OVERSIGHT AND STRUCTURE,
Washington, DC.

The Subcommittees met at 10:03 a.m., in room SD–534 of the Dirksen Senate Office Building, Senator Connie Mack (Chairman of the Subcommittee on Housing Opportunity and Community Development) and Senator Lauch Faircloth (Chairman of the Subcommittee on HUD Oversight and Structure) presiding.

OPENING STATEMENT OF SENATOR MACK

Senator MACK. Good morning, everyone. I just want to thank all of you for being here this morning.

I would like to take this opportunity, our first meeting, to welcome the new Members, whom I assume will be here shortly, to the Subcommittee. I will be looking forward to their contributions as we move ahead to explore ways to better provide housing opportunities to our Nation's families and to restore our communities.

I am also pleased that this distinguished panel could join us this morning, kicking off the hearing of the Subcommittee on Housing Opportunity and Community Development, and my colleague, Senator Faircloth's Subcommittee on HUD Oversight and Structure.

We are here today to focus on the mission, management, and programs of HUD. We intend to explore the various proposals to restructure or possibly eliminate the agency in order to improve the delivery of housing services to American families and revitalize our neighborhoods.

There is a lot of talk, as all of you know, about a range of proposals that are out there that go to the extent of even talking about the elimination of HUD. I think it would be wise for everyone to understand that even individuals who are talking about the elimination of HUD are not talking about the elimination of providing assistance to the people of our Nation who need that assistance.

I am reminded every time that we hold hearings about housing about my own experiences in my own State, of trying to make myself knowledgeable about the problems facing our communities and our neighborhoods and those who are not as fortunate as we. There is one particular situation that I recall very early on in my own personal education of the issues facing public housing and low-in-

come housing in the country. I was in Melbourne, FL with the public housing folks there, and we went to visit one of the public housing communities. It seems like we are always visiting those communities where there are problems. I remember walking down—this was not a 6- or 7- or 10- or 12-story building, it was a 2- or 3-story building, but yet you can imagine what it looked like through the eyes of, say, a 3- or 4-year-old. There is a fellow by the name of Eddie Taylor who was with me. Eddie was pointing out this young boy, about the age of 3 or 4, and units that were in total disrepair, some windows boarded up, a number of units not being used except by those who were using them from time to time to sell drugs. Eddie's comment to me was, "Can you imagine what the dreams of this little 3- or 4-year-old boy must be when all he can see is what you see right now?"

Well, I don't have to go into details because you've all seen it. But my point here is, our interest in these hearings and our interest as we work our way through the hearings on housing is in fact to find a better way to provide assistance for those in our Country who need it.

I would hope that those who hear and participate in this process don't too quickly point a finger at those of us who believe that we ought to try to find another approach, point a finger at us as if we were mean-spirited or have no compassion for our fellow man, because that's just fundamentally false.

During these hearings we will examine the role of the Federal Government in meeting the Nation's housing and community development needs. We will start by assessing HUD's mission and its capacity to carry out its mission with the organizational structure and management systems now in place. In doing so, we must ask hard questions about the various programs HUD oversees. The basic question should be, if we weren't already doing this program, would we start it up in today's fiscal climate, knowing what we know about its performance? If the answer is no, then we should eliminate it. If the answer is yes, then we must find another way.

While I am not yet committed to any specific solution, I am committed to finding serious answers to those questions, then taking the necessary steps to implement them. The viewpoints that will be presented today represent a spectrum of ideas about the future of HUD and its programs, ranging from maintaining the Department and its mission to streamlining and consolidating its many programs, to eliminating the agency altogether.

There is no doubt that HUD faces an enormous number of complicated problems. We are beginning today to seriously rethink Federal housing policy and decide what is the appropriate new direction to take. Whether or not this debate leads to reorganization of HUD or some other means for providing for housing and community development needs, something must be done, and the time to act is now.

Given the budgetary climate in which we now operate, we can no longer afford housing programs that are poorly targeted, grossly inefficient, excessively costly, and poorly managed.

I hope that today's hearing and the upcoming hearings on this subject will provide us with some innovative ideas and solutions to the problems facing communities and families. Any solutions must

return a measure of control to governments that are closer to the people and operate without excessive Federal intervention.

For purposes of today's hearing we have divided the witnesses into two panels. I plan to limit each panel to one hour.

The first panel will begin with Judy England-Joseph from the General Accounting Office; Susan Gaffney from the Office of the Inspector General at HUD; and Jacqueline Rogers, who is representing the National Academy of Public Administration.

Our second panel includes John Weicher from The Hudson Institute; Anthony Downs from The Brookings Institution; and Ron Utt from The Heritage Foundation.

Each witness is asked to limit their oral presentations to 5 minutes. Full written statements will be made part of the Committee record.

We wish to thank all the witnesses here today for their time, interest, and willingness to share their views on the future of HUD.

At this time I would turn to Senator Faircloth for any comments he might have.

OPENING STATEMENT OF SENATOR FAIRCLOTH

Senator FAIRCLOTH. Thank you, Senator Mack. I am delighted to be here this morning and pleased to be co-chairing the hearing with you.

I also wish to welcome the witnesses and hear what they have to say. I intend to be very brief so that we can have time to hear what they have to say.

This hearing is the start of many examining the role of HUD and its future. As you all well know, HUD was created in 1965, and when it was created the purpose of the Department was to revitalize urban areas and provide housing for low-income Americans. In my opinion, it has been a dismal failure. Since 1965, HUD has spent hundreds of billions of dollars, yet our cities are worse off, homelessness as a problem has grown, public housing has been a nightmare for many poor families, and home ownership is down.

Solving these problems was supposed to be HUD's mission. But as I said, it has been a miserable failure.

I also have no faith that HUD can be "reinvented." In fact, it has been reinvented several times, and the invention always seems to be just a duplication of the problems that were in the old HUD.

If Mr. Cisneros really believed in the reform plan he has put forward, he would have started it 2 years ago, not wait until the Department was up for abolishment, to put together the second or third or fifth reinvention plan.

Most important to this Committee, HUD is a spending machine that has no end in sight. I think this Nation as a whole and the Congress, whether Democrat, Republican, or whatever—but as a Nation, we have come to face the reality that our economic resources are not infinite, and we simply have to control our propensity to consume and spend. For example, HUD has told us that they are saving $13 billion over 5 years. This simply isn't so. In reality, HUD will be spending $11 billion more over the next 5 years based on their 1995 spending level. So it's going up rather than down.

This Committee has given HUD budget authority to spend $192 billion over the next 5 years. I think we need to move quickly now to stop the spending and redirect the spending, but to stop it from going into the old and conventional HUD ways. For this reason, I introduced S. 435, a bill to abolish HUD by 1998. I was pleased to see that Senator Dole endorsed the effort.

I want to reiterate what Senator Mack just said, that this is not mean-spirited; this is not an effort to deprive the truly needy of a place to live or decent housing; but it is an effort to correct an agency that over the years has simply proven the direction and the way it is doing business doesn't work, and we have to find newer and more innovative and better ways to look after the needs of the people that have the need for low-cost housing. But HUD hasn't proven that it can do it.

I look forward to the witnesses' testimony today, and I want to solicit your thoughts and opinions and ideas on what we can do to better use the taxpayers' money to provide clean, adequate, and decent housing for those least able to afford it, which is truly our effort, not to perpetuate some bureaucratic monstrosity that HUD has become.

I thank you, Mr. Chairman.

Senator MACK. Senator Bryan.

OPENING STATEMENT OF SENATOR BRYAN

Senator BRYAN. Mr. Chairman, thank you for holding this hearing today. I have a couple of very brief observations so that we can hear from our witnesses.

I think irrespective of which side of the aisle you sit on, there is a recognition that there are some very serious structural problems in HUD. They have occurred in previous Administrations, Democrat and Republican alike. Many of us on this Committee are receptive to change, recognize that there are better ways that we can do things, certainly consolidate some of the programs, streamline the bureaucracy and, frankly, take a critical look at some of those programs that simply are not working, well-intended as they were, but are simply not working. I would like to associate myself with that point of view.

I want to make just a couple of very brief observations about the FHA program. That is something that is near and dear to my heart. Each of us who comes to the Congress brings our own experiences, our own perceptions. And I must say that one of the more exciting moments of my youth was in Las Vegas at the corner of 10th Street and Charleston Boulevard in the fall of 1943. Our family made arrangements to acquire our first home; FHA was the agency that made that possible. I didn't begin to understand what FHA was, did not begin to understand what was occurring other than the fact that there was a plat map, and one of those pins represented our home, and we moved in there. That was a big day in our lives. It's a big day in people's lives today to own their own home. They in effect realize a part of the American dream which, I think, for most of us, is home ownership.

So I am very concerned, Mr. Chairman, when we talk about making changes in FHA, I'm not resistant to taking a look if there is a way that we can make those programs work better, but I think

the agenda of some is to privatize that program. Although FHA, for my family and tens of millions of families in America, made the difference. I will resist this. And that is one bias that I bring to this Congress and to this discussion on how we reform HUD. I look forward to working with you, Mr. Chairman, and other Members of this Subcommittee and the full Committee and the Congress to see if we can't make HUD a better and more responsive institution. I certainly embrace many of the changes that are being discussed.

Thank you very much.

Senator MACK. Thank you, Senator Bryan.

Now we will turn to our panel.

Ms. Joseph.

STATEMENT OF JUDY A. ENGLAND-JOSEPH, DIRECTOR, HOUSING AND COMMUNITY DEVELOPMENT ISSUES, U.S. GENERAL ACCOUNTING OFFICE; ACCOMPANIED BY: DENNIS W. FRICKE, ASSISTANT DIRECTOR

Ms. ENGLAND-JOSEPH. Thank you very much. I appreciate the opportunity to testify before you. I am accompanied by Dennis Fricke, who is also with the General Accounting Office. He is an Assistant Director, responsible for some of our low-income housing work.

This morning we're talking about HUD and a lot of the longstanding concerns that HUD has had, and many of us have had, regarding HUD's capacity to effectively manage its programs. HUD drives huge loan commitments and discretionary spending. Couple that with its longstanding management problems, and it means that today is the appropriate time to fully examine HUD's mission, to determine how well HUD serves its clients, how effectively it carries out its mission and role in Government, and whether that role ought to continue.

To do that really raises a much broader question, and that is a full examination, perhaps, of our Federal housing policy, because beyond HUD there are a number of other Federal agencies that have responsibility for housing.

Let me just take a brief moment to give you an overview of the management and budgetary problems at HUD, those that we have spoken about in the past, four longstanding problems: weak internal controls; an ineffective organizational structure; an insufficient mix of staff with the proper skills; and inadequate financial and management information systems.

HUD's slow progress in making improvements in this area caused GAO to name HUD as an entire Department a "high risk" back in January 1994, and a couple of weeks ago we issued our first report describing the progress that they have made.

HUD's problems create a particularly vexing problem for the Congress and for HUD. HUD expects to lose $10 billion as a result of defaults in their multifamily portfolio over the next 6 years. Multibillion dollars in costs continue in the rental housing subsidy area for millions of low-income families, creating a tremendous strain on the Congressional budgeting process. And to maintain public housing in its current form, we are faced with billions of dollars in backlogged housing rehab needs, increased vacancy levels, and declining tenant incomes.

Now, HUD has taken some steps and begun to address many of these problems. They are all in the early stages and there is quite a long way to go to make the kind of progress that I think we'd like to see.

Solving HUD's problems will neither be easy nor quick, and in fact, they are tremendously complex. However, unless housing policies are substantially changed or revised, the budgetary issues that we've mentioned and the problems that we've talked about will remain extremely high for the foreseeable future. So it really begs the question, what shall we do about HUD?

Now, some thoughts about implications of restructuring HUD. HUD currently serves millions of low-income Americans with rental subsidies, many of whom—over half—are elderly or persons with special disabilities. They also make home ownership more feasible. They address housing discrimination, and they help revitalize communities.

Given management and budget problems, though, it is clear that serving these same customers with existing delivery systems does not work, is not working, and major reform—perhaps radical reform—is needed. But really, no matter how mild or how drastic the reform, there are serious budgetary and social implications. I know the Secretary has described to you his Reinvent Blueprint. We have certain issues or concerns about that Blueprint.

Some of the most radical changes to the existing programs that they propose are in public housing. Recognize, however, that a large percentage of the residents in public housing are elderly and with special needs, not likely under any scenario to become self-sufficient, a cornerstone of the proposal in the Administration's Reinvent Blueprint.

For some public housing with projects in good condition, the Reinvent Blueprint proposal could provide a financial windfall, allowing public housing authorities to raise rents that, through tenant-based vouchers, would be paid for by the Federal Government, thus costing the Government more money at the project level than what we pay today.

In the community development area, the biggest change that they would foresee is blocking—using the model of the Community Development Block Grant—blocking a number of programs. The biggest issue there is the development of performance measures that recognize local needs and local conditions, but also allow adequate assurance at the national level so that Federal dollars are spent appropriately.

The other thing, based on work that we have done in the community development area, is a question among a lot of community development advocates on the inability or ability to quantify results in any sort of community development arena.

In transforming HUD, which is the third part of the HUD Blueprint, we really need to talk about, first, who do we want to serve by continuing FHA? Do we want to serve a narrow, perhaps yet riskier, market niche not currently served by the marketplace today? Or do we want to serve a broader market niche that then would have FHA competing with the rest of the conventional market?

I think a bigger question in the single-family area is, do we need an FHA for single family?

In the multifamily area, the question really needing to be addressed is associating HUD's role in the capital marketplace in trying to increase the flow of capital for multifamily housing construction. In addition to that, the existing condition in the multifamily area causes us to really look at the marking-to-market proposal that HUD has proposed. Is it the most practical? Is it cost-effective? Is it the most cost-efficient approach to solve the problem? Are there alternatives? And for those alternatives, are they any less risky than what HUD has proposed? Do we even know enough about this portfolio of multifamily properties to know whether we can make a truly rational decision?

Having said all that, I would commend the Secretary for developing a thought-provoking, perhaps debate-provoking, proposal; however, the Blueprint does lack a lot of details. I think that it presumes a continuation of HUD's current mission, one that I still question, whether that should be on the table.

In addition to HUD's current mission and questions raised by the Blueprint, I think we would pose a question. Do we need a HUD? If not, should other Federal entities or Federal agencies take on HUD's responsibilities? If so, which ones, and how effectively could they carry out those missions? If not a Federal entity, then we're probably talking State and local governments, and again I think the question is capacity, the ability of State and local governments to carry that role forward. I think the speed with which that implementation could occur needs to be addressed, as well as any sort of questions about oversight, whether the Congress really wants to assure any degree of confidence about expenditures at the local level.

Now, if we carry these questions a little bit further to the assisted housing area, an area that I think merits the greatest amount of attention because three-quarters of HUD's budget really addresses the public and assisted housing areas, there are really two overarching questions. Can significant savings be achieved through a reinvention or a reorganization of HUD?

A reorganization could save some dollars, but primarily that's through administrative savings. It really doesn't affect the bottom line appropriations. To realize significant budgetary savings, we really are talking beyond the reinvention of HUD to really changing the way in which we provide subsidies to low-income people.

I think the Congress is faced with some very difficult questions. We will need to decide how many people should we serve, how much assistance should poor people receive, and for how long. That's very difficult, again, because we deal with a very difficult population. It's not homogeneous. There are elderly, there are persons with disabilities, there are families with children.

Many of these questions need to be answered. Whether they are answered at the Federal level or are chosen to be answered at the State and local level is another issue that I think the Congress would need to decide.

If you keep HUD, how quickly can you expect HUD to transition and to fully implement any new housing assistance programs? As I mentioned to you earlier, the longstanding management problems

that GAO has seen over the last 10 years indicate to us that progress typically is very, very slow. And even though we commend this current Secretary for the amount of effort and energy that has been placed in trying to restructure HUD, and also trying to get behind a lot of these longstanding problems, we're really talking about 2 years of effort and a long, long way to go before we see substantial improvement in place.

But the ability to act quickly is further affected by program design issues—not HUD design, but program design issues. In order to restructure the multifamily loan portfolio, it really means analyzing every single property in that portfolio to really determine exactly what we need to do and what is the most cost-effective approach to doing it. At the current pace in which we are analyzing that portfolio at HUD, it could easily take us 20 to 30 years.

In the Section 8 new construction and substantial rehab area, HUD is contractually obligated to provide subsidies to hundreds of thousands of units. There the decision to move is one that is affected by contracts, not by speed. Between now and 1999, only 14 percent of the units under these contracts will expire. That means that many of your abilities to make decisions on these subsidies really carry you into the year 2000 and beyond, to 2020.

Senator MACK. Ms. Joseph, are you about to wrap up?

Ms. ENGLAND-JOSEPH. Yes, sir. This is my last sentence.

The bottom line is, even if we were to abolish HUD today, hundreds of billions of dollars in commitments stretching beyond the year 2020 mean that the Federal responsibility will not disappear, nor will the costs associated with supporting that. So you have some very difficult questions posed in front of you.

Thank you, sir.

Senator MACK. Thank you.

Ms. Gaffney.

STATEMENT OF SUSAN GAFFNEY, INSPECTOR GENERAL, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT; ACCOMPANIED BY: CHRIS GREER, ASSISTANT INSPECTOR GENERAL FOR AUDIT

Ms. GAFFNEY. This 5 minutes rule is a real challenge.

[Laughter.]

Ms. GAFFNEY. I would like to introduce to you Chris Greer, who is our Assistant Inspector General for Audit.

I would just like to say a couple of things to start off with. You know, I'm always very negative, and that's because I'm an Inspector General, but I need to tell you, HUD does some things reasonably well. The insurance of single-family mortgages is one of them. The tenant-based Section 8 vouchers is another. There are some 3,000 housing authorities, and I've seen a lot of them that are in good shape. They are not Chicago and they are not New Orleans and they are not Detroit, but a lot of those housing authorities are out there doing a good job.

Senator MOSELEY-BRAUN. We're trying. We're trying.

[Laughter.]

Ms. GAFFNEY. So with that as background, I will now talk a more normal IG-kind of talk.

We've given you a comprehensive written statement that backs this testimony up. I'm going to be very brief.

The letter of invitation raises major policy issues about HUD. That's not really the forte of the Inspector General. We're not supposed to get involved in policy issues; our focus is implementation.

However, I would say to you that, on the broad policy level, there are two things that I really think you should be concerned about. One is, you need to rationalize HUD housing assistance and welfare reform, the shelter allowance under welfare. I don't have a position what that relationship should be, but it should be put on the table and rationalized.

The second thing that I would say at a policy level is that we're supposed to be concerned here about needy people and helping poor people and lifting them up, and housing is just one way to do that. I think the other big issue that we need to face up to—and GAO has just issued a report on this—is the need to bring Federal agencies together so they are not all operating in cylinders, with turf becoming the predominant thing that they're interested in while trying to help people.

In public housing, for instance, when you see the proliferation of programs, well beyond housing into social programs, it is because there is a perception that the other programs that are supposed to be providing those social services are not doing that within public housing.

So, that's the end of my policy comments.

In terms of the Reinvention Blueprint, we certainly support important aspects of it. It's about time. It's been a long time coming. HUD has realized that it cannot manage the broad range of programs that it has, and consolidation, simplification, and providing more flexibilities to States and local governments are therefore good ideas—although I don't think that anyone should think that State and local governments are pure as the driven snow and that the Federal Government is the only entity that mismanages things. But if we have good performance measures, this should work, and we're all for it.

The Reinvention Blueprint also faces up, finally, to two huge problems that HUD faces. One is large troubled public housing authorities, and the other is a very troubled multifamily housing portfolio.

We have some cautions for you about this Blueprint, though. One is that the Blueprint was announced almost simultaneously with a major cut in HUD staffing and a cut in S&E funding. This was the $800 million reduction over 5 years. I am aware of no attempt to relate the Reinvention Blueprint with this staffing cut. I say to you, I know Federal workers are not popular, and I know cutting Federal workers is popular; but we should do things in a way that makes sense. My reading of the Reinvention Blueprint is that in the transition years, more effort—not less—is going to be required because, you see, in these transition years they are proposing to solve all these huge problems that have gone unaddressed all this time.

A second caution about the Reinvention Blueprint is, as Judy said, it is lacking in details, and particularly it is lacking in cost data. So, it's almost impossible to figure out how much this is going

to cost or how much it is going to save us, and obviously those are huge considerations in two areas. One is the public housing transition from public housing project-based to vouchers or certificates, and the other one is this concept of marking-to-market in multifamily. Obviously you need data and you don't have it, and I'm running out of time.

Senator MACK. You can take a couple extra minutes. You go ahead.

Ms. GAFFNEY. All right.

The third caution about the Reinvention Blueprint is that right now you have to question HUD's ability to implement it based on current performance.

As you consider this Reinvention Blueprint, I would ask you to consider doing two other things as the policy debate moves forward. One, would you please consider doing some legislative reforms that would simply help us clean up HUD programs in the interim? You know, we didn't have consensus a lot of things last year. We seem now to have consensus on, for instance, that the one-for-one replacement rule in public housing doesn't make a lot of sense. There are a whole series of things like that that you could do, and I think you could do it easily and move forward so that we don't wait forever until we get the "grand vision." I note that, in the House rescission package, for instance, they have included repeal of one-for-one, so that's good.

The second thing I would say to you is that you need to convey—and we in the OIG are trying to convey—to HUD that there are things that HUD can do right now to lay a groundwork for major improvements. HUD can do these things without waiting for interim legislative reform or for the great vision of a new HUD. For instance, large troubled public housing authorities are in fact a disgrace in this country. HUD has broad authorities to move against those public housing authorities. It's a very politically sensitive issue, and so we tend to lack the will. I think you need to tell HUD to go at it, not to wait until you finish your debate.

Another example—my final example—is that the whole Reinvention Blueprint, the marking-to-market dealing with this troubled multifamily housing portfolio, implies that we are going to have information to make informed, rational decisions. We don't have that information. So what would make a whole lot of sense right now for HUD to do is to move full steam ahead and make that a huge priority so that when you make your policy decisions, whatever they are, we are ready to move.

Thank you, Mr. Chairman, Mr. Chairman.

Senator MACK. Thank you very much.

Ms. Rogers.

STATEMENT OF JACQUELINE ROGERS, SENIOR FELLOW, UNIVERSITY OF MARYLAND, SCHOOL OF PUBLIC AFFAIRS, ON BEHALF OF THE NATIONAL ACADEMY OF PUBLIC ADMINISTRATION; ACCOMPANIED BY: AL KLIMAN, FORMER HUD BUDGET OFFICER, ROGER SPERRY, DIRECTOR OF MANAGEMENT PROGRAMS, NATIONAL ACADEMY OF PUBLIC ADMINISTRATION

Ms. ROGERS. Thank you, Mr. Chairman and Members of the Committee. My name is Jacqueline Rogers, and I was a member of the panel on the Future Organization and Management of the Department of Housing and Urban Development for the National Academy of Public Administration. Until January 1995, I served for 7 years as Secretary of the Maryland State Department of Housing and Community Development, and I am now a Senior Fellow at the University of Maryland School of Public Affairs. With me today are Al Kliman, who was the project coordinator and is known to many Members of this Committee, and Roger Sperry, who is the Academy's Director of Management Programs.

The Academy is a private, nonprofit, and nonpartisan organization which was chartered by Congress to improve the effectiveness of Government at all levels—Federal, State, and local. Last year, pursuant to a Congressional mandate, the panel completed an analysis of HUD, including the Department's human resource requirements and management, financial management, systems integration, and resource estimation capabilities. The study's scope also included an assessment of HUD's organization. The panel's final report, "Renewing HUD: A Long-Term Agenda for Effective Performance," was issued in July, 1994.

The Academy panel addressed the fundamental issues of how to simplify and consolidate programs and sustain management attention on building and maintaining HUD's institutional capacity. In so doing, we focused heavily on how the Federal Government can relate to communities in a more constructive manner. Copies of the panel's report have been provided to the Subcommittees, and I request that the summary report be included in the record of this hearing.

After reviewing the evidence, our panel concluded that HUD is at a crossroads. It can become a very effective public institution, or it could continue down the now-familiar road of poor performance. Our panel concluded that if, after 5 years, HUD was not operating under a clear legislative mandate and in an effective and accountable manner, the President and Congress should seriously consider dismantling the Department and moving its core programs elsewhere.

I want to stress two things in this basic message that we had for you. The first is that we found the problem in HUD operations to be a jointly-shared problem between the Legislative and Executive Branches. HUD's mandate—witness the one-for-one rule—definitely interferes with its orderly performance, so there are problems that need to be addressed on both sides of the street.

The panel made its statement because of the underlying problems requiring further attention by both the Administration and Congress. This was not intended as an indictment of HUD's current leadership, whom we found to be both capable and qualified.

In fact, we found that the current leadership was moving proactively on several fronts to address many of the long-standing management deficiencies which are described in our report.

We said, however, that there must be some basic changes in underlying legislation, and there must be a management agenda within HUD to develop the skills and the information necessary to function more effectively.

The Administration's reinvention proposal that Congress will soon have before it in legislative form will trigger dialogue on the comprehensive program reauthorization that our panel was seeking. The proposal to consolidate about 60 programs into three large block grants directly responds to our call for program consolidation and simplification. Certainly, this consolidation will help HUD interact much more effectively with State and local governments to deliver programs and services.

The proposal to convert the Federal Housing Administration into a Government corporation is also responsive to another of the panel's recommendations. We feel it is very important for this vital agency to preserve its mandate to serve that portion of the market which is not being accessed by conventional mechanisms, while at the same time being able to manage the business of risk in a businesslike way, which is very difficult to do in its current structure.

The panel did not consider the current proposals that are on the table relating to public and Indian housing, so I can't speak on behalf of the panel with regard to those issues.

The causes of HUD's underlying problems are not all found in one place. As the NAPA report sets forth, there was a lack of political consensus when Congress established HUD, and there is no consensus today on what it is, or should be, as a Department. A part of the problem is what the report calls an "expectations glut" where the rhetoric surrounding the Department, coming from both the Executive and Legislative Branches, set up expectations far in excess of what HUD is authorized to do or could do with the resources that are available.

If HUD is to function effectively, the Administration, the Department, and Congress need to proceed expeditiously with comprehensive reconsideration, consolidation, and reauthorization of HUD's core programs. Until the programmatic house is in order, no amount of tinkering with management will cure what ails this organization. Our panel recommended that HUD's program structure be consolidated into no more than 10 major programs. In the meantime, as Susan suggested, HUD should have additional waiver and demonstration authority to provide needed flexibility in meeting the varied needs of State and local governments and other housing providers. There is presently nothing in the authorization legislation that gives HUD the freedom to experiment with success.

Now that HUD has proposed to rationalize its program structure and make FHA a Government corporation, it is Congress' turn to act on a comprehensive reauthorization of the programs operated by HUD. We are concerned, however, that further reducing of staff in HUD in advance of program streamlining and consolidation could continue the mismatch between statutory requirements and available resources. We recommend that HUD develop a long-term management agenda to accompany reforms in the program agenda.

A sensible and flexible legislative structure, program consolidation, management improvement, and appropriate resource levels are all needed to make HUD an effective institution, and this is what our panel was striving for.

I have attached to my testimony a summary of the panel's major conclusions for your future reference.

Before closing, Mr. Chairman, I would like to invite the Members of the Committee in my old capacity as a State official to take some time to visit Maryland, because we have in Baltimore City fine examples of the kind of public housing that you as a group decry. But we also have outstanding examples of where Federal programs have worked to serve the people and improve their lives in other parts of the State, and it troubles me personally, deeply, that so much emphasis is placed on failure and so little attention is placed on what is truly succeeding for people in our communities. There are many communities that are no more than half an hour's drive from here where you could see HUD's programs serving people effectively.

Thank you very much.

Senator MACK. Thank you. Again, I want to thank all the panelists. I know that you have been involved in these issues for a long, long time. I have heard you speak on these issues in the past and you all do so eloquently and passionately, and for that I thank you.

My intention at this point is to recognize Senator Kerry, and then Senator Moseley-Braun, both of whom are Ranking Members of the two Subcommittees at this hearing, and then we will proceed with our questions.

Senator Kerry.

OPENING STATEMENT OF SENATOR KERRY

Senator KERRY. Senator Mack, thank you very much. My apologies for not having been here at the very opening of the hearing. Regrettably, March madness is not just basketball; it's everybody coming to Washington, and somehow they were all in my office this morning. So I apologize for not being here at the start.

Senator SARBANES. Some of them were in my office.

[Laughter.]

Senator KERRY. I have no doubt that they're in every office. This is the flood.

Mr. Chairman, thank you for holding this hearing. I just want to say publicly for the first time as we meet, beginning this journey, what a pleasure it is to work with you and the other Members of our Committee. You and I have collaborated in the past and I think we have worked well together, and I certainly look forward to continuing that good relationship and collaboration into this effort.

I know some of my colleagues, as staff have informed me, have appropriately signalled criticisms for an agency that, for obvious reasons, is easy to criticize. There are some very large housing authority problems and individual instances of disaster that are very easy to focus on. I would just like to take a moment, if I may, to sort of lay the groundwork for where I hope we're going to journey. I have talked to Senator Bond privately, and I look forward to

working with him and Senator Mikulski on the appropriations side to see if we can join our efforts here.

We are about to consider the most radical overhaul of the Nation's housing programs that has been undertaken in many decades. I think as we do that, it is important to remember the journey traveled, what brought us here. There was a time in this country when the Government played very little role in housing, Senator Faircloth, and I think you remember back to that time. There were limited housing codes. There was no Government involvement in the production of affordable housing. There was no intercession in the marketplace to make mortgages available for young families, and there were no efforts to make sure that senior citizens had a place to live in their senior years.

In that America, hundreds of thousands of Americans lived in the most squalid tenements. Few families could look forward to the promise of home ownership, and the elderly often lacked a decent home during the final years of their lives. For the first 160 years of this Nation's independence, housing markets in the United States had the opportunity on their own, left to the free enterprise system, with no Government interference—they had the opportunity to provide decent housing for America's citizens, and the result was, quite literally, a national disgrace.

In the 1930's, America decided they were going to change this situation. During that decade and in succeeding decades, through both Democratic and Republican Administrations, we established public housing authorities to build, own, and operate affordable housing, including thousands of units to house returning veterans and their families.

In the effort to unleash the creative energy of private developers, we did establish some subsidy and insurance programs to encourage the production of affordable housing in our big cities and in rural areas. I think that you might say that in point of truth, the great depression gave us public housing, and the riots of the 1960's gave us subsidized housing. And we should not forget those riots, nor should we forget what laid the groundwork for that subsidized program.

It was in the wake of those urban riots of the 1960's that we established the agency to oversee these efforts called the Department of Housing and Urban Development. That is an agency whose promise has often exceeded its accomplishments, although its accomplishments should not—as Ms. Rogers appropriately said—should not be understated.

In America today there are over 6 million affordable housing units which exist, in part, due to the activities of this agency, and the vast majority of these are well-managed and maintained. I would point out to my colleagues on the other side that out of some 3,400 public housing authorities in the country, there are probably only 15 to 30 that fit into the kind of disaster category which is used to sully the entire effort. And indeed, we ought to do something about those, and I will have suggestions as we go along as to how.

But it seems to me that we should not forget that thousands of senior citizens and people with disabilities who cannot move easily in a program of vouchers are today in decent and safe housing, and

a far cry from the conditions that they encountered during the years when no role existed for the Government in the housing markets. Whole neighborhoods have been restored to strength, notwithstanding the signal monuments to failure—whole neighborhoods all across this country that we don't hear about in the news every day have been strengthened by carefully-targeted investments that combine public and private dollars in partnership, where the private dollars would not go alone for lack of a bottom line sufficient to empower the money to move there, or for other fears.

Now, I am prepared to admit the failings. You would have to be an idiot not to today. HUD has tried to micromanage certain affairs of local government, often without improving the local performance in a measurable way. Thousands of units today are in disrepair or vacant, without any clear target date for renovation. During the previous two Republican Administrations, HUD programs were, frankly, shamelessly bilked to provide unearned profit to private developers at the expense of the recipients for whom these programs were designed, and the number of programs ballooned well beyond the capacity of HUD staff to manage and oversee. I might say that we recently saw some 17 indictments as a consequence of that period of management.

Today is the day to radically restructure HUD, what it does and how it does it, but it is not the day to eliminate all Government involvement in that effort to provide decent, safe and sanitary housing for all Americans, and not the moment to simply shift it to one type, i.e., vouchers, to the exclusion of other programs that work.

I believe that our approach should give individual States and cities the power to spend Federal funds in the way that is most useful to their own circumstances, but making sure that they meet clear Federal guidelines, including equal housing opportunity and the avoidance of displacement. It is, I think, our responsibility to make sure that we spend this money in a way that benefits those greatest in need and not just for the primary benefit of landlords and developers.

We should also recognize that some housing is beyond redemption, and it should be demolished. When such demolition occurs, we ought to try to make the best effort to currently protect those who had been living there, and to replace units that are lost.

We have lowered the income threshold, often in our rush to help those in the greatest need—we have lowered the income threshold for entrance into subsidized housing, creating communities consisting almost entirely of very low-income families, many of whom are unemployed. So we have learned something from that experience, and in the future we should obviously strive to create communities where people of varied means and backgrounds live. In my own State of Massachusetts, the emphasis on mixed-income housing has created some of the most successful communities, and I invite my colleagues to measure those.

Finally, we should take steps to unleash the potential of thousands of community-based nonprofit developers who stand ready to build, renovate, and manage housing which will remain affordable far into the future.

I think that in any reform of this effort we have to take care to protect the affordable housing stock that we've already invested in. This is a resource and we shouldn't simply put it into jeopardy. It obviously means too much to the people who live there today, and to deny it for the future is simply to invite an enormous crisis in this country in the near term, which I promise my colleagues on this Committee we will be back revisiting in short order, examining what we did to bring that calamity upon us.

Most importantly, I think we should not accept on their face many of the unwise ideas which masquerade as reform. For those who believe that the private market, left unfettered, is going to provide for the housing needs of millions of America's poor and homeless, elderly and disabled, there is a 60-year record to provide ample proof that that is simply not the case. So those who are looking to vouchers as the cure to all of this—and incidentally, I think vouchers will work in certain cases, and they will work in certain places—but you cannot simply translate all of these programs into that effort because if priced too low, they simply transfer money from the Federal Government to private landlords, and if priced too high, they can distort the marketplace and result in displacement of current tenants, not to mention a host of other problems.

Mr. Chairman, I just want to say that we need to look very, very carefully at what these programs are going to do. The question of displacement is an enormously important one; 95 percent of the 1.7 million households in project-based Section 8 units today have incomes of less than $7,500 a year. There are certain communities, like Massachusetts and New York, where you simply are not going to find a voucher value sufficient to find housing for those people. We know that ahead of time. One-half of those people are elderly or disabled. They can't vote with their feet, in a sense. They can't take that voucher and easily go out and find that new location. The impact on the industry could be a disastrous effect on the FHA insurance fund, not to mention on State housing finance agencies and any private lenders. You would have a great increase in default rates and foreclosures on already-FHA-insured property, FmHA-financed projects, and you could have huge write-downs and a whole impact on the marketplace that obviously has to be measured, not to mention the impact on bond ratings and on future lending.

So my plea to the Committee is that, yes, there are management difficulties. The worst of the programs are really the 236 and 202, the big FHA insurance-based programs. We've got expiring use; we've been through that in the last few years. We clearly need to address the question of how we separate those terrible units from those that work. And maybe we want to think about something along the lines of what we did in the banking situation, where we literally took the bad banks out. Here we may want to leave the good and take the bad out and deal with that as a "bad bank structure."

But I would invite my colleagues to please measure history and experience here. We don't need to reinvent the wheel of crisis yet again. We have learned in these years that some of these programs do work. We have learned how to make mixed housing work. We have learned how to create smaller units. We have learned through

the disasters in Chicago, in Massachusetts, in New York and elsewhere, that we can do a better job.

So, Mr. Chairman, that's a long introduction and I apologize in one sense for it, but in another I don't because I think it's very important to lay the marker down for how we're going to proceed here. I am prepared to do a radical overhaul. I am prepared to look at innovation. I am prepared to be open-minded. I am certainly not wedded to the past, but I do not want to ignore the realities of the marketplace and realities of what we have achieved as we approach this very, very important effort.

Senator MACK. Thank you, Senator Kerry.

Senator Moseley-Braun.

OPENING STATEMENT OF SENATOR MOSELEY-BRAUN

Senator MOSELEY-BRAUN. Thank you very much, Mr. Chairman. I am going to be brief and I would also like to associate myself with Senator Kerry's remarks, because I think he makes a very important point.

I would like, however, to just touch on a few things.

The first is that the 1934 act called on us to provide for every American decent and safe housing. That was the direction we took; that was the commitment we made to the American people. So there is no question, as Senator Kerry has pointed out, but that the goals of the 1934 act really have never been met, but it is as much to the point that our attempts to meet those goals have been fraught with difficulty over time.

I therefore join Senator Kerry and others in suggesting that perhaps we do need to reorganize and take a look, support the Secretary's efforts to reorganize, and take a look at revisiting the way this agency does business, and the path that we should follow in order to reach the goals of the 1934 act.

Excuse me. I have the flu, Mr. Chairman. I'm doing the best I can.

Senator MACK. You're doing fine.

Senator MOSELEY-BRAUN. Let me say this, Mr. Chairman. Reform of this agency does not mean retrenchment from the goals of the act. Reform of this agency does not mean that we turn our backs on decisions made in 1934 to provide every American with safe and decent housing. That seems to me to be a fundamental kind of commitment to the American people that we should not turn our backs on. We should not allow our zeal for reform to represent a backing-off of that fundamental commitment so that we wind up with greater homelessness, poorer standards of housing, less decent housing, less safe housing, and that we really create a crisis where one need not be created. That's my first observation.

My second observation is that—Senator Kerry talked about this point—HUD is a resource in jeopardy, and in that regard it is in large part because of the failures of the past, but it is a resource nonetheless, and it has provided us with the ability to address some of these issues on a broad scale, whether the issue is financing of private housing under the FHA program, or the issue is maintenance of public housing, or Section 8 vouchers, or housing for people with AIDS—you know, you can go right down the list, and HUD is the vehicle with which we have addressed these is-

sues. It seems to me that, again, while you fix your car when it's broken, you don't take the engine out altogether and just absolutely disable it. We can do the kinds of fixing, we can do the kinds of reform, we can begin to fix the particular aspects of this agency that are in need of repair without totally disabling our capacity and our ability to use this resource to address the housing of the Nation.

The third issue I would like to raise—and I look at this panel, at these three witnesses—there are two huge gaps here that I see. The first is in terms of the private sector. There is no question but that any elimination of HUD would have dramatic effects on the real estate market. I don't know to what extent we have private sector in mind when we talk about what does this do to the real estate market, the reform of HUD or even some of the more radical proposals to eliminate HUD altogether—what impact will that have on the real estate market and the kind of ripple effect from any action that we take here?

The issue, also, of the secondary market ought to raised, to take a look at what the elimination of HUD would mean. Does that mean we would no longer have a Government organization? Would we have a Government-sponsored organization involved in the purchase of paper in the secondary market? I think we need to be able to fully look at the implications in terms of the private sector. This panel does not reflect that perspective, but I'm sure that we'll have a chance to move on and to further get into those issues.

Finally, with regard to the second group, that I think we absolutely, positively need to hear from, it has to do with people in State and local government. The fact of the matter is that the rescission package that came over from the House can have a dramatic impact on State and local governments. If State and local governments, because of our actions here, wind up with bigger problems in terms of financing and development of housing, bigger problems in terms of providing low- to moderate-income housing, larger homeless populations, then those are costs that they will have to pick up. In this body we have recently been very taken with the notion of not passing on to State and local governments what are called unfunded mandates. I fear that a lot of the conversation about what we do with HUD will result in a huge unfunded mandate for State and local governments that, quite frankly, they are not all that anxious to have visited upon them without some concession from the front end.

So I would make those recommendations, Mr. Chairman, that we need to take a look at the impact on State and local governments and take a look at the impact on the private sector, but at the same time work together in a bipartisan fashion in order to achieve the kinds of reforms that this agency needs without having to flinch from our commitment to have decent housing options available for the American people.

Senator MACK. Thank you for your comments.

Senator Bond.

OPENING STATEMENT OF SENATOR BOND

Senator BOND. Thank you very much, Mr. Chairman. I very much appreciate your holding this hearing, and the distinguished Ranking Members.

This panel has been before our VA-HUD Appropriations Subcommittee because Senator Mikulski and I have the dubious distinction of having to act within the next week or so on a rescission package, and then we're going to have to start work on an appropriations package. The suggestion has been made here by Inspector General Gaffney that there are some short-term fixes, like the one-for-one replacement rule. I think there are some short-term things that we need to get to work on. I believe that the witnesses here today have given us a very good outline of the problems that we face. We want to work with the Banking Committee, Members on both sides, to develop the long-range solutions to these problems.

I just want to tell you today what we are seeing on our preliminary investigation, because we need to make sure that we go in the appropriations process in a way that is consistent with where this Committee is going to go in the authorizing process, and again, no finer witnesses could start off the hearing.

HUD is dysfunctional. The best organization in the world couldn't do a good job of administering 240 separate programs the way Congress has set this up. In addition, HUD has brought in their own problems. They have created—they continue to create—problems in this new era as they come forth with "streamlining." You find that they keep slipping in programs that haven't been authorized. That's got to stop. There has to be drastic surgery. But unlike some of my colleagues, I'm going to be very clear: I don't believe that it is possible to eliminate HUD totally, because HUD has long-term financial commitments and obligations, and they are carrying out some responsibilities that I don't think the people of America are ready to see the Federal Government junk. I think the Federal presence can be effective. There are certain basic housing and community development needs which can be addressed. I think we can do it much better, by and large, relying on State and local governments to do it, but I don't think we need to pass along some of the tremendous financial burdens that have been built up to State and local governments.

The best you can say about the President's budget for fiscal year 1996 is that it offers little in the way of hope. The President's budget says that they are going to increase the HUD budget by $20 billion in BA and $14 billion in outlays over the next 5 years. I don't know who they're talking to, but they're not talking to the same budget committees and appropriators that I'm talking to.

In addition, besides not having that money that they say is necessary, they have the fallacy that has been addressed by Ms. Gaffney of claiming a $1.7 billion savings for marking-to-market, just wiping out the value of some of the projects that have been built with project-based Section 8 certificates, and nobody has the foggiest idea how much that's going to cost. Nic Retsinas said that in a memo in January, and we don't know how much that's going to cost. If that weren't enough, last week, I understand, the Congressional Budget Office said that the President's budget has underestimated the cost of HUD housing and community development

assistance by some $27 billion over the next 5 years. Now, that is a headache of a magnitude that we're going to have to deal with. We have to deal with short-term. We need to get some things through. I think one-for-one replacement is very important. And the rescission package, frankly—I see that the House rescinded funds for tearing down distressed housing. I think that's one of the best investments we can make. We can't stop tearing down distressed housing, because that leaves the communities with the eyesores, that leaves them with burdens they can't handle.

I am going to offer a much longer statement, believe it or not, for the record——

[Laughter.]

Senator BOND [continuing]. So that you——

Senator MACK. That would be a relief, I might say.

Senator MOSELEY-BRAUN. That's what I tried to do.

Senator BOND. Hey, listen, mine's still green.

Any reform needs to keep housing over the heads of tenants who are receiving it. We need to protect the existing housing stock. There's no way we can do that and voucherize. That just doesn't make any sense. We must consolidate into far fewer programs. I like the target that Ms. Rogers said of 10. We need to rely on State and local governments. I think a post-audit function only, letting HUD come in—the ultimate sanction is to have HUD pre-approval or to have HUD take over in receivership. By and large, let the State and local governments run it. I would do a public housing block grant, and if the public housing is well-run, keep HUD out of it; assisted housing block grant with Section 8 funding to the States and the localities; community development and home block grant, with 40 percent to States, 60 percent to entitlement communities, with a 25 percent match requirement—that's one of the only ways we can get there—and a post-audit function. I would retain Section 202 elderly housing, and tell HUD, "You have to separate the Section 11 disabled tenants from the Section 202." They still haven't gotten the message. I would keep the HPWA program. I would conduct a top-to-bottom review of FHA, move the Office of Fair Housing and Equal Opportunity to the DOJ, and the Office of Federal Housing Enterprise to the Treasury.

Senator MACK. I see you've managed to hit the red light.

[Laughter.]

Senator BOND. And you will notice that, unlike others, I have stopped at the end of a sentence. And here's a longer statement for the record, but I do look forward to working with you.

Senator MACK. Thank you, Senator Bond.

Senator Sarbanes.

OPENING STATEMENT OF SENATOR SARBANES

Senator SARBANES. Thank you very much, Mr. Chairman.

First of all, it is obvious that this and subsequent hearings to follow are very important in the examining of a very significant question. I have been interested in hearing the comments of my colleagues because I think they reflect a range of thinking about this situation in which we find ourselves and how to address it. I hope we will be able to go through a very careful process of examination and analysis and take a good hard look at the facts in the course

of trying to reach a judgment as to what ought to be done. My own view, of course, is that there is an important commitment that we have to undertake in addressing the Nation's housing problems. I don't think they can be fully met without an involvement by the public sector, and I think our challenge is how to structure that involvement in a way that works well.

I listened to Senator Bond; I thought he laid out a number of interesting issues to be examined. I'm a little uneasy at consolidating the home program into anything, because I do think that the home program is one of the ones that's working pretty well, frankly, and I think they've got a good system for monitoring established. It has succeeded in establishing an important partnership with the State and local governments and the private sector, both for-profit and not-for-profit. It provides a lot of flexibility at the local level to meet local needs and to fill financing gaps in making housing affordable. I think it is building State and local capacity, actually, to provide affordable housing. I think the results thus far have been very good. State and local governments are using the flexibility for diverse housing activities, and they are exceeding the objectives for targeting and leveraging. So I think it is working, actually, to produce some important advances with respect to housing, and I hope we will be sensitive to that as we examine this question.

I am concerned—and I want to state it; I'm not on the Appropriations Committee, of course, but I am concerned—about the rescission package, and to the extent the appropriators are willing to take some signals from the authorizers, I am particularly concerned about rescissions which are going to make it more difficult to stabilize the troubled housing inventory. It seems to me that first and foremost, we need to be concerned about sustaining and protecting the housing inventory that has been committed for affordable housing. I think it's really a foolish policy to take measures that, in effect, will turn out not to be cost-effective in the sense that we will lose that housing, or lose the advances we are trying to make.

The effort to tear down the housing that is so troubled that it is a blight on the community has, I think, a well-justified rationale, and we need to move ahead on it. If we don't, what's to be done? Is it simply to remain there, casting a pall on the entire community, with no alternative?

The effort to take housing that is acceptable but below standard and bring it up to standard, it seems to me that the analysis sustains it as a wise investment.

Now, we, on a bipartisan basis last year, I think put forth a good piece of legislation. I appreciate that there are obviously other matters that need to be addressed, and we may want to go further. We were not able to move that on the floor, but this Committee brought it forth. It had program consolidation and the homeless and the rental assistance areas; most everyone feels there's a need for program consolidation. In fact, the people at the witness table this morning have been very strong on that. It reformed the rent structure in public housing to create an incentive to work and to begin to reverse the increasingly difficult-to-manage concentrations of the poorest of the poor. We've had panels of those who have run good public housing projects in some of our cities, and this was the

thing they most focused upon as enabling them to strengthen their programs. It gave HUD increased enforcement tools to deal with bad housing managers, and, of course, it sought to remedy the distressed public housing programs in various ways.

So I am hopeful that as we move ahead, Mr. Chairman, and as we—here I take it from the Department and others—in the weeks to come, that we will be able to fashion a package that can improve substantially its performance, that maximizes the return on the resources that are being committed, and in effect enables us to keep moving forward in the effort to provide affordable, decent housing to those who otherwise would find themselves in extremely dire circumstances.

Thank you.

Senator MACK. Thank you.

Senator BOND. Mr. Chairman, just let me say that we welcome the advice of the distinguished Ranking Member of the Committee, and any staff comments on the rescissions, if you would provide them to our staff, or if Members want to talk with us—because we have a daunting task. I will just say that I believe the home program is working. I'm talking about expanding the home program and building on it.

Senator MACK. We will now turn to questions.

Ms. Joseph, if I may direct the first question to you. We have panelists here today who suggest everything from abolishing the agency to returning power to the States, to privatizing many of HUD's functions. Based on your work, do you agree that fundamental change is warranted? What, if any, concerns or cautions might you have regarding a redesign of HUD?

Ms. ENGLAND-JOSEPH. Yes, sir. I think we believe that redesign of HUD—or a much broader question about housing policy, and what's the most effective approach the Federal Government may want to take in delivering that housing policy—needs to be addressed.

I think the concern that we have as you all move forward in debating both of those issues, whether to redesign HUD or start from scratch and really develop something different in terms of Federal housing policy, is to be somewhat mindful that we are not dealing with a homogeneous population and a "one size fits all" approach is not necessarily the best approach. It does require us to not only understand the characteristics of the people who we are intending to serve, but also the conditions of the markets in which that housing is or where those people actually live. That is something that is very difficult to generalize. Most proposals tend to generalize on that front. That's where it gets really sticky, and that's where the costs also come into play.

So that's the only caution that I think we would make.

Senator MACK. All right.

Ms. Rogers, the NAPA report has stated that "if HUD's mission cannot be identified and it cannot demonstrate its capacity to manage its resources responsibly, Congress should consider steps to dismantle the agency." I heard you testify to that point several weeks ago at the hearing that Senator Bond chaired.

To what degree has HUD responded to the underlying problems that NAPA unveiled in its report?

Ms. ROGERS. I think the Reinvention Blueprint goes a long way in the direction that the panel was seeking. We felt very strongly about privatization of FHA, that its mandate to serve lower-income households be preserved, and we felt that program consolidation was an absolutely essential component of what had to happen next.

We did not look at the right-to-market proposals that are now on the table, and we did not examine public and Indian housing from the standpoint that HUD is approaching it now. But I think that the Secretary and his senior staff have really grabbed the bull by the horns and are offering a sound foundation for further discussion.

Senator MACK. Are you all concerned at this point at the lack of details, though, with respect to the report?

Ms. ROGERS. It's my understanding—and perhaps Susan is more knowledgeable than I am—that the working papers on what the legislation would contain are at OMB now, and that there will be very detailed legislative proposals available to Congress this month. So we are all waiting to see what the proposals will look like.

I would like to underscore Judy's emphasis that the solution to this problem is not going to be a simple "one size fits all" solution because you have to take geography and demography into consideration before you come up with blanket solutions.

Senator MACK. In what areas do you have concern with respect to HUD not addressing the issues that you all raised? Or did they address them all?

Ms. ROGERS. There are a couple that I'm sure Al would want to speak to. We still think there is room for more sustained attention to management detail.

Maybe, Al, you'd like to take that one on?

Mr. KLIMAN. Yes. Thank you, Jacqueline.

The major point that HUD has not addressed thus far is what we call the management agenda. We feel very strongly that any improvements that are put into effect would be long-term improvements, and that, in effect, was the name of our report, the "Long-Term Agenda."

One of the problems with HUD is that historically, something gets started and then stops again very quickly. We had a number of proposals in the report to provide the organization with a measure of continuity so that to the extent that there were reforms that were proposed, either within the Department or by the Congress, that there would be some institutional capability to carry them forward into the future, and that's one of the major things that has not been addressed thus far.

One other thing of concern, and both Ms. Rogers and the GAO have addressed this, is the question of staff capacity. One of the problems that NAPA recited was that HUD does not have the capacity to administer the programs that it has. We are concerned that in the agenda that has been presented for HUD, the reduction of the staff in advance of program improvements will maintain the same poor performance that we've seen in the past.

Senator MACK. The last point that you were talking about, let me again just address it to Ms. Gaffney, this whole issue about given the current staff situation at HUD, do you think the Department

has the administrative capability and capacity to carry out the reforms? I know that's been raised several times. I guess I want to give one more opportunity for it to be underscored.

Ms. GAFFNEY. First of all, I think my answer about whether HUD has the capability depends on what your program design is, how you define the mission.

Senator MACK. Let me be more specific, then. Assume for a moment that the reform package that they are proposing, do they have the capability and the capacity to carry that out?

Ms. GAFFNEY. I have seen no proposals thus far that would assure me that they are able to carry out major portions of that Blueprint. They may be formulating such plans, but under the current circumstances they couldn't do it, and I haven't seen plans where they would acquire those resources.

Would you like me to give you a couple of examples?

Senator MACK. You've been reading my mind.

[Laughter.]

Ms. GAFFNEY. Well, the Blueprint assumes—and to go back to what a number of people here said about large troubled public housing authorities—there are relatively few of them, but they are huge. And they are the reason public housing has such a terrible reputation in this country. The Blueprint assumes that HUD is going to be able to turn those public housing authorities around in a period of 2 or 3 years. The times are changing in the various iterations, but I'm going with the first draft. Whether it's 3 or whether it's 6 or whether it's 12, you would have to ask: If they can do it in the future, why haven't they done it in the past? And I assume one of the answers is, capacity. So where is the capacity coming from in the future to accomplish this?

Senator MACK. I see that Mr. Kliman apparently agrees with you.

Mr. KLIMAN. Definitely so.

Ms. ROGERS. Senator, this is the same kind of complicated question you're going to face when you deal with larger policy issues. It's obvious that if major program consolidation occurs, and 240 programs—or the current 60 that are now proposed—are consolidated down into 3 major program areas, that liberates a great deal of staff capacity that is now at HUD that is regulating and monitoring tiny little programs that are managed with no help from Washington. So there is plenty of staff capability that will be liberated in that area that could be applied to dealing with some of the other problems that the agency faces.

The second thing is that inherent in the notion of privatizing FHA comes the flexibility to acquire the talent and pay for the talent that has the expertise to deal with troubled properties in a thoughtful way. I think that FHA manages risk, and that's a business function, and as a corporation they would be in a position to staff appropriately to deal with their business functions.

Senator MACK. I'm going to go ahead and move on to Senator Faircloth.

Senator FAIRCLOTH. I want to ask Ms. England-Joseph, Ms. Gaffney, and also Ms. Rogers a question. It will be the same question. As in so many hearings, we are limited in time, so if you will answer it shortly.

Should HUD be abolished now or in the future?

[Laughter.]

Senator FAIRCLOTH. I address that to Ms. England-Joseph.

Ms. ENGLAND-JOSEPH. A quick answer is, it depends.

Senator FAIRCLOTH. That's a good, strong answer.

[Laughter.]

Ms. ENGLAND-JOSEPH. It truly depends, sir, on what you're trying to accomplish with the dismantlement. If you do not see a mission and function in the Federal Government that HUD now typically provides, then in fact you can try to work out an arrangement for its dismantlement. It will not happen as quickly as you would like. If you see a role in Government, then I think we need to decide how would we redesign an organization like HUD, or some other entity like HUD, to carry out Federal housing policy?

Senator FAIRCLOTH. Ms. Gaffney.

Ms. GAFFNEY. I agree with Judy. I think that from my perspective, the question of whether HUD should be abolished or maintained almost doesn't make any difference because in my mind, HUD is a collection of buildings, like other office buildings. It's a collection of 11,000 people who aren't evil; they're just like other Federal workers.

The real question is what Senator Kerry talked about before, and that is, what do we want to accomplish? Once you define that, then I think you should go to the most effective implementation device available. And you can figure that out, and it's not necessarily HUD. Maybe it's having 5 different agencies do the function. Maybe it's having an advisory board or a commission, or maybe it's HUD. But I think you get there at the end of the discussion. Do you understand what I'm trying to say?

Senator FAIRCLOTH. I hope so.

[Laughter.]

Ms. GAFFNEY. I'm not worried about your ability to understand; I'm worried about my ability to explain.

Senator FAIRCLOTH. Ms. Rogers.

Ms. ROGERS. Senator, there is an embedded physical plant and there are Federal commitments that extend out over the next 40 years that have to be dealt with in some fashion by HUD or by any successor agency. And I believe that we need to rationalize how we intend to manage that system, and then you can name it whatever you want to, but I don't think you're going to solve any problems by announcing, "HUD is hereby abolished," because the commitments are all still there.

This is the first time, frankly, in a decade or so that I have seen the will at the Congressional level in the authorizing committees to sit down and sort through fundamental mandate and policy and to try to rationalize systems that are broken, and I commend you for doing that and hope you will stick with it until you can make a good decision about how to manage those commitments.

Senator FAIRCLOTH. Ms. Gaffney, in previous testimony you have suggested that we don't need HUD's Office of Fair Housing. Can the function of this office be transferred to the Justice Department without hindering efforts?

Ms. GAFFNEY. We did a study for the Secretary on opportunities for eliminating, restructuring, and consolidating HUD programs.

Our focus was getting HUD back to its really core programs and getting rid of everything that was not essential to that core. So we recommended that consideration be given to moving fair housing enforcement to the Department of Justice. We recommended that HUD's Indian programs might be considered for transfer to the Department of the Interior, and we recommended that HUD's lead-based paint abatement program be considered for moving to EPA.

I will tell you, we looked at this solely from HUD's perspective, that HUD has so many responsibilities and so few resources that it can't cover the waterfront. To be very honest with you, we did not go to the Department of Justice and assess that move from their perspective.

Senator FAIRCLOTH. You say "has so few resources," i.e., money?

Ms. GAFFNEY. Staff capability. Staff capability. The ability to——

Senator FAIRCLOTH. Well, 11,000 isn't enough?

Ms. GAFFNEY. Well, you define capability in a number of ways. Numbers are one. Training is another. But 11,000 people in relation to the huge workload—it is not just the dollar amount of the budget. It's also what Senator Bond was saying about 240 discrete programs.

Senator FAIRCLOTH. Let me ask you a quick question. Are we doing too much? Are we trying to do too much?

Ms. GAFFNEY. Clearly, the Office of Inspector General believes that is one of the fundamental problems.

Senator FAIRCLOTH. You ought to be doing less?

Ms. GAFFNEY. That we are trying to cover a gamut of activities within HUD programs that HUD simply cannot manage.

Senator FAIRCLOTH. Ms. England-Joseph, we're saying that HUD is cutting, suggested by Secretary Cisneros that they are reducing cutting by $13 billion over 5 years. Is it not true that they are actually spending $11 billion more over the next 5 years, that the level is going up from if you started a baseline of 1995?

Ms. ENGLAND-JOSEPH. Yes, sir. You are right.

Senator FAIRCLOTH. Then where does he say the cutting is coming from? What does "cut" mean?

Ms. ENGLAND-JOSEPH. When you show a trend in terms of if you stayed at——

Senator FAIRCLOTH. If you do what now?

Ms. ENGLAND-JOSEPH. If you show a trend from your status quo programs, your existing, current services, and the growth that normally is attributed to that growth. He's comparing that baseline, not holding solid and firm.

Senator FAIRCLOTH. So you are expanding slower?

Ms. ENGLAND-JOSEPH. Excuse me?

Senator FAIRCLOTH. Is that what you're saying? You are expanding slower?

Ms. ENGLAND-JOSEPH. You are expanding slower. Yes, sir. But you are still spending more money.

Senator FAIRCLOTH. Only in the Federal Government does expanding slower mean cutting.

Senator KERRY. That's not really true. Every business in the country has costs go up. Gas costs more, electricity costs more, health care costs more. There isn't a company in the world whose revenues don't cover that.

Senator FAIRCLOTH. Senator Kerry, I believe I have been in business as long as anybody, and in a lot of them—some big ones and some small ones—and I have never in my life heard of spending more being called spending less.

Senator MACK. Senator Kerry, it is your time.

Senator KERRY. I'm happy to let my colleague go on if he wants to ask some more questions.

Senator FAIRCLOTH. That's all.

Senator KERRY. I didn't say it is spending less. It is a cut. It doesn't matter. We don't need to struggle over this, but the fact is you can cut automatic increases. Look at all of the entitlements that we have—Medicare, Medicaid, Social Security. They are on an automatic increase just because a larger number of people are drawing down on them, a larger number of people get older.

So, in effect, you can still be spending more, but you can be cutting. It does make sense, and it can have a dramatic impact. If you have more people suddenly seeking housing or more units on line, if you suddenly start cutting you may still be spending more money than the fixed amount but you, in effect, are cutting people out of their opportunity or their housing or diminishing.

It works, and I think the Senator knows that.

I think that the key here is to focus on what really happens or is happening.

I'd like to ask Ms. Gaffney and Ms. England-Joseph a question. It is my understanding that, by and large, the distressed projects in HUD today were developed under both Sections 221–D–3 and 236 programs. Is that accurate?

Ms. GAFFNEY. I think they are a large part of it, but Chris is the expert. Let me ask him to answer that.

Mr. GREER. The lion's share is in the Section 221–D–4, new construction, sub-rehab programs.

Senator KERRY. That's the lion's share of problem, isn't it?

Mr. GREER. Yes.

Senator KERRY. OK. So when we talk about the problems we are really talking about this particular program that was—most of that stock, in fact, got in trouble within 2 years of completion, did it not?

Mr. GREER. Yes. It was poorly-designed, poorly-underwritten, etc., etc.

Senator KERRY. Those problems resulted, did they not, essentially from a lack of adequate capitalization?

Mr. GREER. Yes.

Senator KERRY. Also with an excessive focus on a short-term tax incentive, correct?

Mr. GREER. At that time we had tax syndications, accelerated depreciation. Yes, sir.

Senator KERRY. Who made out on that? That went to the developers, correct?

Mr. GREER. Developers and syndicators. It was all fee driven.

Senator KERRY. Correct. Fee driven. It is not as if the management had some inherent inability to manage. There was a tax structure passed that gave an incentive where perhaps it shouldn't have been, correct?

Mr. GREER. Right. But you also had some good and bad managers.

Senator KERRY. I understand that. And you still do, correct?

Mr. GREER. Yes.

Senator KERRY. And we can identify those?

Mr. GREER. For the most part, yes.

Senator KERRY. We also had an inadequate oversight of the private developers during the construction and management, didn't we?

Mr. GREER. Yes, sir.

Senator KERRY. Now, the second major group of distressed HUD-assisted properties got in trouble through disinvestment after they were resyndicated in the early 1980's, correct?

Mr. GREER. Yes, sir.

Senator KERRY. And they then got caught in the consequences of tax reform in 1986?

Mr. GREER. A good share of them. Yes, sir.

Senator KERRY. So you've got not HUD but the U.S. Congress that helped contribute to that problem?

Mr. GREER. Yes, sir. As Susan pointed out in her statement, there are a lot of folks to blame for the situation that HUD is in currently.

Senator KERRY. In specific contrast to those two programs—Section 236 and Section 221–D–3—most Section 8 properties, especially those financed by the high-quality housing finance agencies such as we have in Massachusetts, the Massachusetts Housing Finance Agency, for instance, are in good condition and they are well managed, are they not?

Mr. GREER. We haven't done a whole lot of audit work in that area, but the reading I have done would indicate that you are correct. Yes, sir.

Senator KERRY. And that is because the tax incentive rewards stable ownership, quality construction, and good management. Is that fair?

Mr. GREER. Yes.

Senator KERRY. So it is your perception that there are a set of programs here clearly that we have been able to show why something didn't work and why something does work?

Mr. GREER. What has happened in the past oftentimes is Congress will pass laws without that kind of an analysis, so I think you're right on the mark. Good analysis needs to be done of the various programs.

Ms. GAFFNEY. I would like to say one other thing, and that is there is a great difficulty in doing good analysis, to go back to the same point, because even though conceptually what you are saying makes sense, and Chris is certainly affirming it, HUD does not have comprehensive data that enabled an analysis that all of us could say was absolutely correct.

Senator KERRY. I hear you, but this is pretty fundamental. This is a big amount of money, in the billions of dollars. And these are very fundamental things that we can target that went wrong, correct? We also can target what went right.

On the Section 8, I think most of us would agree that the indexing, the increase, is too high. It is too much, so we need to reign

that in. But these are understandable. This is not something that I find is overly-baffling. We've been at this for a long time now.

Ms. GAFFNEY. And I agree with you. There are a number of things that we could change, that the Congress could change, that there is agreement on that would reduce waste a lot.

Senator KERRY. Let me pursue that, if I may.

It is my understanding that the principal reasons that the past efforts at redevelopment of these distressed properties has failed is the fact that those properties were often sold by HUD after foreclosure with inadequate repairs that were passed on to the buyers.

Mr. GREER. I think that's just one part of the problem.

Senator KERRY. Is it part of the problem?

Mr. GREER. Yes.

Senator KERRY. It is a significant part. If you've got a property, you buy it at foreclosure, but there are inadequate repairs, then you've got a capitalization problem, don't you?

Mr. GREER. Yes. But we would say to you that HUD has not been aggressively pursuing foreclosure as a sanction against bad owners, bad management.

Senator KERRY. I would absolutely agree with you, and one of the great disgraces of a lot of this property is that you have had this property sitting there in this incredible state with the owners continuing to take rent, many of them, I might add, not even paying on their notes but continuing to collect rent.

Mr. GREER. Right.

Senator KERRY. Which is an extraordinary situation, and HUD has allowed that to go on.

Mr. GREER. There are many contributing factors.

Senator KERRY. But none of them baffling, is my point. This is why. I guess what is baffling is why the hell somebody doesn't move on this and manage it a little better. That is baffling, because—go ahead, Ms. Gaffney.

Ms. GAFFNEY. I don't want to take your time, but we could cite 50 more baffling issues where it is pretty straightforward and everybody knows what is wrong and HUD isn't taking the action or the Congress is not.

Senator KERRY. This is exactly what these hearings are about. I'd like to get those 50 more examples, frankly.

Mr. GREER. Fifteen, I think.

Senator KERRY. Fifteen or 50?

Ms. GAFFNEY. I said 50, but we have outlined, for instance, in our testimony——

Senator KERRY. Would you submit them for the record to the Committee?

Ms. GAFFNEY. Sure. Absolutely.

Senator KERRY. Would that be all right, Mr. Chairman?

Senator MACK. Absolutely. We'd be very much interested.

[Information to be supplied follows:]

Ms. GAFFNEY. Many of them are mentioned in our statement.

Senator KERRY. I see my light is on.

Senator MACK. My intention is to move to the next panel, so if you want——

Senator KERRY. I guess I can submit some of these questions for the record, Mr. Chairman. I don't want to tie us up. But let me just ask a couple of quick ones if I can.

Ms. Gaffney, what is the impact of the $7.2 billion in recision by the House Appropriations Committee on HUD's ability to address the management difficulties and problems it faces?

Ms. GAFFNEY. We have not done that analysis. I'll tell you our general position on the budget has been to fund HUD's core programs. Our general view is you have no choice, you must, and the comments that have been made here about public housing—for instance, demolishing the structures that are a disgrace, getting the stuff back into some decent shape—it seems to me make a lot of sense.

Our position has generally been: if you can cut funding for ancillary programs, what are sometimes called "boutique programs," which are not essential to the core of HUD's mission, that's where you should cut.

I know it is not popular, but we've got a big Section 8 problem on our hands from a budget perspective, and I think you would look at incremental vouchers as one of the first things that you would hold back on in a time of budget crunch.

Senator KERRY. Let me just ask you, there is such a knee-jerk response around here so often, and I'm wondering if cutting 4,400 employees over the next 5 years is a legitimate response to a quick capacity to get rid of excess, or is that going to just contribute significantly to the current problems? Do you want to both answer that?

Ms. GAFFNEY. Please let me.

Senator KERRY. That's why I'm asking you.

Ms. GAFFNEY. I can assure you that HUD has no system in place for assessing what its staffing needs are or allocating staffing resources. To my knowledge, there is no basis for that cut in staffing at all.

I believe if HUD were reinvented according to that Blueprint in 6 years or 3 years, or whatever it is, maybe HUD could get by with 50 people. That's conceivable. I don't know.

But it is clear to me that in the transition years HUD is going to need more resources, not fewer.

Senator KERRY. Ms. England-Joseph?

Ms. ENGLAND-JOSEPH. I would suggest to you, sir, that the 4,000 number came about not in relationship to the Blueprint and the implementation of the Blueprint, but probably simply to show some dollar savings in a quick fashion.

What you have is a very serious problem in the multifamily portfolio, Section 8 new construction, sub-rehab that you were referring to earlier in your questions. HUD is saying it does not have the capacity today to deal with that problem, and that it will require actually new contract authority and new S&E—salaries and expenses—in order to hire the kind of resources, either permanent or temporary, in order to meet that current need.

Senator KERRY. That certainly presents us with a serious confrontation with reality, and just one more piece of this mosaic that we need to think about.

Thank you, Mr. Chairman. I appreciate it.

I would submit some questions for the record.

Senator MACK. Certainly.

Again, I thank the panel. We'll move on to the second panel. Thank you all very much.

Again, I want to thank the panelists for taking your time to be with us this morning. Why don't we start with Mr. Weicher.

STATEMENT OF JOHN WEICHER, SENIOR FELLOW, THE HUDSON INSTITUTE, FORMER ASSISTANT SECRETARY, OFFICE OF POLICY DEVELOPMENT AND RESEARCH, HUD FOR SECRETARY JACK KEMP

Mr. WEICHER. Thank you, Senator. And thank you for inviting me to appear today. I'm especially glad to be here because this year offers a real chance to reform American housing policy.

I want to start by saying that I'm not here to speak for the Hudson Institute or for anyone else but myself.

I have been at HUD in three different Administrations, most recently as Assistant Secretary for Policy Development and Research with Secretary Kemp from 1989 to 1993. Twice I came to HUD in the aftermath of scandals. I am an economist, and I have specialized in housing and urban issues throughout my career.

In my mind, the best way to begin thinking about HUD's future mission and how to reform it is to look at what HUD does now, what it does well, what it does badly, and why.

To start with what HUD does well: This is a short list but it is an important one.

First is FHA home mortgage insurance. FHA serves the basic public purpose of helping young families buy their first home. It could be better targeted by limiting it to first-time buyers and to families in the lower half of the income distribution, but it serves home buyers that are not yet served by private mortgage insurers, and it serves them without losing money.

Second, the voucher and certificate programs. These help over one million low-income families pay the rent on decent private housing of their own choice—all kinds of people in all kinds of markets. Over half of the recipients are African-American or Hispanic. This is the most cost-effective housing assistance program we have.

Third is the community development block grant. CDBG gives money to State and local governments to address neighborhood problems or community facilities or economic development.

These are established programs. FHA home mortgage insurance was created 60 years ago, vouchers and CDBG were both created 20 years ago in the same act. They have worked reasonably well for a long period of time.

What does HUD do badly? This will take a little longer.

I'll start with FHA multifamily insurance, which does lose money. FHA has had to establish a $10 billion loss reserve on a $44 billion portfolio. The budget projects a loss of $0.07 on every $1 of multifamily insurance that FHA issues this year. That's on top of the $0.05 mortgage insurance premium.

Multifamily insurance is difficult to underwrite. Every deal is unique. It is very staff intensive. FHA's portfolio is about 90 percent single family and 10 percent multifamily, but the staff is split

50/50. And there have been recurring scandals going back to the Section 608 program in the late 1940's.

The problems are compounded when FHA insurance is combined with subsidies to build low-income projects—when we're dealing with the "insured assisted inventory." There is pressure to underwrite these projects generously, to make them work, and then there is pressure to provide generous subsidies to support the mortgage. Still, many projects get into financial difficulties. When that happens, FHA never wants to foreclose on them. That would be a loss for the insurance fund and then FHA would have to manage the project.

The alternative is further subsidies. The more subsidies there are, the more complicated the program gets. And as the subsidies pile up they offer increasing opportunities for abuse and scandals, as in the Section 8 Mod Rehab Program which kept the Oversight Committees busy a few years ago. These are also the programs where HUD has had the worst management problems and the poorest information and accounting system.

I put public housing on this side of the list also, although it certainly has a mixed record. Most PHA's provide decent housing, but there are troubled PHA's in many of the largest cities, and in most of these cities there are some projects that are locally notorious as terrible places to live.

Public housing is twice as expensive as vouchers or certificates. It costs $85,000 a unit to build, and there are operating subsidies and eventually modernization on top of that.

Based on this experience, I believe that any reform of housing policy and any reform of HUD should be based on what HUD does well—FHA home mortgage insurance, vouchers and certificates, CDBG. At the same time, the Federal Government should stop doing things that it does badly—FHA multifamily insurance and project based assistance in both public housing and privately owned projects. Above all, the Government should stay out of the tempting quagmire of combining multifamily insurance and project based subsidies.

I know it sounds drastic to propose terminating FHA multifamily insurance, but I don't think it would have much effect on the multifamily market.

FHA now accounts for less than 10 percent of the market by any measure. In 1993, 7 percent of the apartments built were built with FHA insurance, only 9,000. That's not much of a presence for all the headaches it causes.

It is certainly possible to make these changes and abolish HUD in the process, splitting up these three functions among other agencies, but since HUD runs these programs reasonably well right now, I don't see any good reason to move them. It is not likely they'll be run much better in another agency, and if other agencies run the same programs that HUD is now having trouble with, I think it is likely the other agencies will have the same problems.

It is more important to change what the Government does in housing in an urban policy than to change where it is done. If Congress changes what HUD does in the way I have suggested, you will really reform HUD and housing policy and you'll help homebuyers and poor families and the taxpayers in the process.

Thank you again for inviting me to testify. I see I am inside the red light.

Senator MACK. You did very well.

Mr. Downs.

STATEMENT OF ANTHONY DOWNS, SENIOR FELLOW, THE BROOKINGS INSTITUTION, WASHINGTON, DC

Mr. DOWNS. It is a privilege to testify before you today on why the Nation should retain a separate Federal Department for Housing and Urban Development.

My qualifications to speak have been set forth in a separate biographical statement, but, as John did, I have to say the views I will express are solely my own and not necessarily those of the Brookings Institution or its trustees. I have said that so often I believe they don't have any views.

The Nation needs a separate Department of Housing and Urban Development to perform two basic functions. One focuses on the provision of adequate housing for the Nation's citizens. The other, which is much less widely realized, focuses on improving the overall special efficiency with which activities in our metropolitan areas are conducted.

First, housing. This is the single costliest element in people's basic living standard, yet millions of households with low-incomes cannot afford to occupy decent quality housing if they have to rely solely on their own resources. If the Federal Government is concerned with its citizens' basic wellbeing, it must be concerned with improving the quality and quantity of their housing—especially that of poor citizens.

But no other agency within the Federal Government focuses on housing as part of its central mission. So no others are likely to pay enough attention to housing to improve the chance that most citizens will be well housed.

Today 13 percent of all renter households in the country are living in units assisted by HUD. That's a fairly significant part of the population.

Why not leave this element to State and local governments? Providing housing aid to poorly housed citizens amounts to redistributing resources from others to those citizens. But all resource redistribution schemes are much more effectively financed, although not necessarily managed, at the Federal level than at the local level. Local governments cannot tax their better off citizens highly in order to aid their poor citizens without causing many of the better off to move away to nearby communities that have no such schemes. Even State governments suffer from that competitive disadvantage. Right now, there is sort of a competition among States to see how much they can cut spending on these programs rather than expand it.

Furthermore, the cost of a household's financing on home purchase is heavily influenced by mortgage interest rates and mortgage fund availability, which are determined by national financial conditions and markets, not State and local ones.

Similarly, the racial and ethnic discrimination and segregation that permeate American housing markets cannot be dealt with ef-

fectively by purely State or local agencies for the same reason that the civil rights movement ultimately required Federal action.

HUD's other central mission, which is far less normally thought about, I believe, relates more to urban development patterns than to housing itself.

About 80 percent of Americans live in more than 330 metropolitan areas, where the basic economic, social, and other functions of American society are carried out. The special efficiency of how activities function within these areas is of vital importance to our whole society. Unfortunately, current trends are seriously undermining that efficiency.

The fragmented local government structure in nearly every metropolitan area makes it impossible to develop coherent, consistent, and effective policies for its several growth-related problems. These include air pollution, other environmental degradation, traffic congestion, provision of sufficient infrastructures to accommodate growth, selection of sites for regionally necessary facilities like airports that have negative impacts on their immediate surroundings, and the absorbance of excessive open space.

All these problems are essentially regional- and metropolitan area-wide in nature. But they are all effected by the patterns of land uses controlled by fragmented local governments. Moreover, each local government is competing with all the others to capture activities that generate net local tax revenues and to reject activities that generate net expenses. This fiscal competition makes creation of a single coordinated land use policy among the local governments in a region virtually impossible.

Even more important is the deteriorating fiscal and social condition of many major central cities and older, close-in suburbs. As rapid growth on the fringes of each metro area draws the most prosperous and viable households and firms out of central cities and older suburbs, those communities are left with declining per capita tax bases and increasing concentrations of poor households with high public service needs.

In 1990 the Nation's central cities contained only 31 percent of the total population, but 42 percent of all poor persons in the country. This concentration of poverty is aggravated by the exclusionary policies of many suburban governments. They erect zoning, building code, and other regulatory barriers to the creation of any added low-cost housing within their boundaries in order to keep "the wrong kind of people" out of their neighborhoods.

Their policies load local governments in older cities and suburbs with increasingly unbearable fiscal burdens and extensive areas of deteriorating or abandoned neighborhoods.

Furthermore, central cities and older suburbs contain a majority of Members of two minority groups, African-Americans and Hispanics, who will play ever-more important roles in the Nation's future. Together, the 58.3 million persons in those two groups comprise 22 percent of the country's total population today, but they will make up 56 percent of the total growth in population between 1995 and the year 2020.

At present, the average household incomes of these minority groups are between 30 and 40 percent below those of non-Hispanic

whites, and the average educational attainment of the former two groups is also low.

Unless this condition is changed, most of the Nation's future population growth will occur among its poorest and least-skilled minority groups. To improve their incomes and skills, American society needs to improve the quality of education and job opportunities available in the central cities and older suburbs where most of these groups live. But that will be extremely difficult if continued future peripheral growth and the outward flow of resources from our metropolitan areas to the edges keeps on draining economically strong households and businesses out of central cities and suburbs.

Right now, no government or private groups anywhere within our society except HUD are officially entrusted with the mission of thinking about or doing something about these adverse trends within our metropolitan areas. Even HUD has not focused much of its past attention on developing policy responses to those trends. Yet somebody with a broad perspective and considerable authority must do so if our country is to compete globally and retain minimal social cohesion.

Certainly HUD, alone, cannot solve all the problems associated with declining cities and deteriorating inner-city neighborhoods. At best, it could not do so without enormous help from many other parts of society. Nor does the need for HUD to exist imply that it should remain in its present form or do business in the same old way. But if HUD does not exist in some form to at least focus public attention on these issues, few, if any, remedial policies will be directed at them. I believe that would be a national tragedy.

Thank you.

Senator MACK. Mr. Downs, thank you.

Mr. Utt.

STATEMENT OF RONALD D. UTT, VISITING FELLOW, THE HERITAGE FOUNDATION, WASHINGTON, DC

Mr. UTT. Thank you, Mr. Chairman and Members of the Subcommittee. Thank you for inviting me to be here today to present my views on HUD's fiscal year 1996 budget proposal and also to discuss possible alternative directions that housing policy might take to better serve those in need.

Let me begin by saying that the views expressed today are mine alone, and do not reflect those of the Heritage Foundation, where I am now a visiting fellow.

In the interest of time, my remarks here today are summarized from a somewhat lengthier statement that I have already submitted to the Committee, and I request that it be included in the record.

By way of introduction, my background in the housing area is a rather eclectic one, beginning originally at HUD in the early 1970's where I was part of a team brought in from around the country in the wake of a series of costly failures and scandals.

Subsequently, I worked on related housing and real estate policy issues at the Office of Management and Budget, and later with several real estate and business trade associations and think tanks in the Washington area.

Most recently I have been a direct participant in the housing market as a licensed general contractor specializing in the acquisition, renovation, and resale of residential housing.

I'd like to begin my statement this morning by commending Secretary Cisneros for a program that, at least in spirit, represents a major break with the patterns and practices of the past, and which proposes to redirect HUD resources in more productive ways, chiefly by favoring household-based assistance over the more costly project-based assistance.

Also commendable is the proposal for an orderly withdrawal of direct Federal support from public housing and the proposal to provide existing residents of public housing with the resources necessary to exercise their choice in housing.

Unfortunately, this year's budget proposes an unnecessarily long time for implementation, and this should be substantially shortened.

In contrast to these positive initiatives, the Secretary's proposal for a new affordable housing fund which would perpetuate under different names the more-costly project-based assistance, and the new entrepreneurial FHA, which appears to steer FHA away from what I believe is its most valuable mission and for a whole host of new, potentially risky missions and partnerships. These latter two I don't find very appealing.

Several years ago, at a different time, the successful implementation of HUD's primary proposals would have marked a significant and positive change for HUD policies. But times change and new opportunities emerge. I believe the resources now controlled by HUD could be more effectively used if they were combined in a social welfare block grant to the States, with governors and mayors authorized to determine the extent to which these resources are to be used for housing, direct income assistance, child care, job placement, etc., within the context of a series of guidelines designed to move low-income households from long-term dependency to self-sufficiency.

At present, and with most of its resources targeted to households with low- to moderate-incomes, HUD is an integral part of the U.S. welfare system, and as such should be an integral part of any solution—one that contains powerful incentives to self-sufficiency rather than the costly dependency creating custodial function that the system, including HUD, performs today.

My colleagues at the Heritage Foundation have had a long involvement of developing effective welfare reform plans, and I would be pleased to have these materials provided to the Members of the Committee if they so wish.

Included in this block grant would be the funds representing approximately 80 percent of HUD's budget, which now go toward a variety of means tested housing assistance programs, including public housing, Section 8 new construction and renovation, as well as Section 8 vouchers and certificates, the old Section 236 programs, and other remnants of past subsidy programs.

I recommend that the low-income housing assistance funds targeted to these programs be combined in a single welfare block grant used at the discretion of the governors.

To the greatest extent possible, what direct housing assistance is provided should be provided through household-based arrangements rather than project-based programs, except in special cases such as the elderly and disabled where cost and quality of life issues are competitive with that provided by way of vouchers.

Moreover, with regard to the existing public housing projects, more encouragement should be provided for tenant- based solutions, including both tenant management and tenant ownership programs that are now in existence but poorly funded relative to the interest in these programs.

Such a proposal is not as extreme as it would appear relative to current arrangements. At present, much of HUD's housing and community development assistance, including vouchers and certificates, are provided to eligible beneficiaries by way of local housing authorities who, under my proposal, would now be acting on behalf of their governor rather than HUD.

In this regard, most of the remaining 20 percent of HUD's budget is for community development block grant programs, which would be made redundant by the welfare block grant proposed above and should be terminated.

Of the remaining major programmatic areas, I recommend that FHA be converted into a financially self-sufficient, independent Government corporation with the responsibility of assisting creditworthy households of moderate incomes to acquire their own homes on an unsubsidized basis that does not jeopardize the financial health of the insurance fund.

In a concluding note, it should be recognized that any major changes in programs such as those operated by HUD must take into consideration the extensive array of long-term financial commitments that HUD has made to a variety of private and public entities that provide different types of housing assistance to eligible households. Cost-effective mechanisms consistent with the overall goal of comprehensive welfare reform must be implemented to ensure the orderly transition from one type of housing assistance to another.

Thank you.

Senator MACK. I thank you for your testimony.

Mr. Weicher, let me address a couple of questions to you, if I could.

As an economist, what do you think would be the potential impact of terminating project-based subsidies in favor of tenant-based subsidies on the banking bond, security, and affordable housing markets if this were to occur immediately?

Mr. WEICHER. I think you cannot terminate all project-based assistance immediately because you have contracts in place. You could terminate public housing operating subsidies because you appropriate them on a year-to-year basis, but the contracts for the privately owned projects expire every few years and so they will come up, they will actually come up for renewal, over a 15-year period.

I think that what will happen, if your focus is on the private side, is that the families who are in those projects, if they are given a voucher or a certificate, some of them in the well managed projects will be happy to stay put. Some of them in the poorly man-

aged projects will be happy to move. Families which wish to move because their circumstances have changed will have the opportunity to move without losing their subsidy and, like the rest of us, they can pick where they want to live and work out whatever deal they can with the private landlord to afford to live in whatever housing they can afford, with the help of the Government so they can afford decent housing.

I think that's the first and most important thing—that you free up the rights of individual low-income citizens to find housing just like the rest of us do instead of telling them where to live and sticking them some place.

I think that what will happen in the financial markets is that the financial markets will simply adjust to whatever changes are made. Some projects are probably going to go into default. HUD has, as I said, a reserve of $0.25 on the dollar now—$10 billion out of $44 billion—on the multifamily insurance that it now has in place. Most of that is multifamily insurance for assisted projects. HUD is already expecting to lose $0.25 on the dollar on those mortgages. I don't know how many of them they are expecting to default, but that's a loss of $0.25 on the dollar, not a default of 25 percent of the mortgages.

So I think the effect of moving to tenant-based assistance is going to be minor in financial markets. I think some landlords will default on their mortgage. HUD will take over the property. And then I think HUD should sell the property as quickly as it can without FHA insurance and put it into the private housing stock.

Senator MACK. I couldn't help, listening to your response, getting the sense that one of the fundamental issues here—and not too many people really want to talk about it—is with project-based you are, in essence, holding those people hostage. Anybody who spends any time at these facilities that are in total disrepair wonder why in the world or how anyone would remain. The reality is they have no choice. So you are suggesting to us that we really ought to give those people choice, which I happen to agree with.

Mr. WEICHER. That's right, and I think many people will not choose to move. In many public housing projects and many private projects the housing is perfectly decent and people will not choose to move, but some will, and they all ought to have the right.

Senator MACK. Let me just follow up on that whole thrust of the first part of my question.

One key aspect of transitioning from project-based to tenant-based assistance is giving both public housing authorities and privately owned project owners time to take steps to compete in the market. It comes back into the same issues, though.

You advocate making the shift immediately. Do you think that public housing authorities, private owners, tenants, investors, and insurers will be able to implement such a significant change without a transition period?

Mr. WEICHER. I think that you should have the transition period after you have changed the policy and changed the programs. Otherwise, I think you could come 3 years down the road and you will be no closer to fundamental reform than you are now.

I think if you compare the budget submitted by HUD to the reinvention Blueprint of last December, they don't quite look like

they are driven by the same policy vision, and I think the reason is that the Blueprint has these long phase-ins for the really fundamental reforms.

In looking at the budget, I am reminded of a prayer of St. Augustine's in the "Confessions," "Lord, give me chastity and continence, but not just now." Don't reform me yet. Wait. I think you have to start the reform process now if you hope to see it in any reasonable period of time.

Senator MACK. Thank you.

Why don't I go ahead and turn to you, and then I'll have some other questions.

Senator FAIRCLOTH. Thank you, Mr. Chairman.

I think the hearings are worthwhile and they are giving us a view of where HUD has been and where it needs to go.

Mr. Utt, do you think that we should abolish HUD and return housing function to the States?

Mr. UTT. Yes, sir.

Senator FAIRCLOTH. In your opinion, how much less expensive would HUD be if it assisted tenants directly as opposed to these housing projects?

Mr. UTT. That's very difficult to answer because we know that on average project-based assistance is twice as expensive as vouchers—sometimes more than twice as expensive. But we know that's an average.

Out there, there are probably a lot of very well-run, very efficiently managed public housing projects that are as cost-effective as vouchers. There are a number that are probably 5 or 6 times more expensive than vouchers because of the care and dilapidation and condition and extra attention that they require.

So we don't know how much we are going to save by lopping off from that system some of the worst of the projects.

Senator FAIRCLOTH. What would you guess?

Mr. UTT. I would guess that simply by terminating the community development program, which assists people very indirectly and very inefficiently, from my perspective, would save $4 or $5 billion per year.

Senator FAIRCLOTH. Mr. Weicher, do you think we should abolish HUD and return the housing to a function of the State?

Mr. WEICHER. No, Senator, I don't. In this I agree with Tony Downs that the income redistribution function is best financed at the Federal level, and I think the voucher and certificate programs which HUD runs and which are, indeed, run by public housing authorities for HUD in most cases, do a good job in helping low-income families find decent housing.

I think I would leave the things that HUD does now with HUD doing them.

Senator FAIRCLOTH. Do you think it would be less expensive—I'll ask you the same question—if we assisted the tenants directly and just got rid of the housing projects?

Mr. WEICHER. Yes, it would. It would certainly, since every new unit that you pay for in public housing or a private-owned project is going to cost double per unit per year to help a family compared to a voucher or certificate. If you convert the units you have now, in public housing and in project-based assistance, to vouchers and

certificates over time, you're going to come out about even as of right now on public housing and you are going to save money on the privately owned projects because the subsidies in the privately owned projects are generally above the fair market rent and can go up to 20 percent above the fair market rent.

If I may say this, the trend on operating subsidies and modernization is like this—rapid growth. The trend on vouchers and certificates is like that—slow growth. Vouchers and certificate costs go up with the rate of inflation; that's a couple percent a year, operating subsidies and modernization now are doubled in real terms what they were 15 years ago, and 15 years ago operating subsidies were being blamed on the energy crisis.

Senator FAIRCLOTH. Let me ask this. There seems to be a general line that I pick up here that is developing that we are talking about destroying, taking down these projects that are eyesores. How old are they? In New York how old are these housing projects we're talking about taking down? How long have they been there?

Mr. WEICHER. The specific projects—I've seen a specific list of projects that you talked about. I think most of them are——

Senator FAIRCLOTH. The youngest. The newest.

Mr. WEICHER. The newest are probably no younger than 20 years old. The oldest——

Senator FAIRCLOTH. And we're talking about taking them down?

Mr. WEICHER. The oldest might be 50 to 60 years.

Senator FAIRCLOTH. But we're talking about—wait a minute. Have we been building housing projects 60 years?

Mr. WEICHER. Close. Since the late 1930's. At least 55 years. Between 55 and 60 years.

Senator FAIRCLOTH. But some of these are 20 years old and we're talking about tearing them down?

Mr. WEICHER. That's an estimate. I don't know the history of all of the projects which HUD has listed here.

Senator FAIRCLOTH. I know you don't.

Mr. WEICHER. The ones I do know in Chicago—Cabrini Green has been there over 40 years. It has been there since I was living there and going to school there.

Senator FAIRCLOTH. Mr. Downs, you favor keeping HUD.

Mr. DOWNS. Yes, sir.

Senator FAIRCLOTH. But if you had to give it a performance rating, kind of based on school grading of A, B, C, D, over the last 30 years what would you grade it at?

Mr. DOWNS. First of all you have to look at the challenge which HUD is facing. A batter who——

Senator FAIRCLOTH. I didn't ask you how hard the course was. I said what would you grade them?

Mr. DOWNS. I think the grade that's given depends on how hard the course is. A batter who bats 333, which is one-third, is considered to be an excellent hitter because it is very difficult to hit a baseball. In the case of public housing, to house the lowest income or almost lowest income 1.4 million households in the country, who are forced to live together by policies that Congress and local governments have made, is a very, very difficult task. So you would not expect HUD to do very well at that, and it has not done very well—even though a lot of public housing is very successful.

I'd say I'd give HUD a C+.

Senator FAIRCLOTH. Let me ask a question that hasn't been asked here, and I'll ask it to any one of the three that want to give me an answer. I am old enough to remember when there was no public housing and was pretty much all over New York and a lot of the major cities. I did not see the dire circumstances that have been mentioned by others here today. What would happen—and we've seen the chaos that public housing has brought to so many areas. What would have happened if we had never gotten into it, maybe private ownership more with FHA, but never touched public housing? What would we have today?

Mr. DOWNS. In Chicago, where I lived for most of my life, the infamous Robert Taylor Homes were built in the 1950's and 1960's. I saw the dwelling units that they replaced, which were cardboard shacks packed together at higher density than the Robert Taylor Homes now have, even though they are high-rise structures.

I would say that for the first 15 years of those projects people were much better off living in those public housing units than they were in the previous units.

Senator FAIRCLOTH. I guess you're right there. You say for the first 15 years? I'm talking about: are they better now living in that project than they were before they were built, I'll say in the late 1940's?

Mr. DOWNS. But then a change in policy occurred. Instead of having working class families with two parents residing in those units, by a combination of HUD policies and legal forces requiring the very poorest people to live in them, you got a concentration of poor single parent households living in them. That's what makes living in some public housing projects disastrous. It isn't the physical structures, it is the character of the people who are living in them who are concentrated together in these areas.

Senator FAIRCLOTH. One quick question and then I'll surrender, Mr. Chairman.

I have trouble because the answer gets so involved that I've forgotten the first part of it before we get to the second part.

Were these people better off in 1952 before these projects were built living as they were than they would be living in this project today? Yes or no?

Mr. DOWNS. No.

Senator FAIRCLOTH. They were not better off before? They'd be better off living in this project today?

Mr. DOWNS. That's right.

Senator FAIRCLOTH. Than they were in 1952 and 1953?

Mr. DOWNS. If they are the same people. The character of the people in projects has changed.

Senator FAIRCLOTH. What?

Mr. DOWNS. The people living in those neighborhoods have changed in character. If the same people lived in the slum neighborhood that I saw in the 1950's were living in those projects today, they'd be better off today than they were then.

Senator FAIRCLOTH. Was there more crime in these neighborhoods in 1952 than there is today?

Mr. DOWNS. No, but that's true of the country generally, not just these neighborhoods.

Senator FAIRCLOTH. Do you think housing projects have had a tendency to proliferate and increase crime?

Mr. DOWNS. In those large projects that concentrate many broken families together, yes, I do.

Senator FAIRCLOTH. I give up. The light's on.

Senator MACK. Let me just make one comment.

I happen to share the same feeling that Mr. Downs has indicated with respect to what has happened to public housing communities. One of the more significant changes that was made had a dramatic effect on public housing communities, when you really encouraged others to live elsewhere and ended up with very, very difficult situations.

I guess a thought comes to my mind. In Miami I had the opportunity to visit, I think, what is, if not the first, probably the second public housing community built in the country, and there is a lady there that I met who was there when it was constructed. She said in no uncertain terms, with a very, very strong sense of anger about the destruction of her community because of this concept of so narrowly defining the criteria under which someone could live in that public housing community.

I happen to share that view. We may not agree on every point, but we do on that one.

I want to turn my attention to Mr. Utt, because you have said in your statement something that I have been trying to wrestle with, and that is: Why don't we set up providing assistance to those who need it with them being the focal point, as opposed to the separate governmental agencies that can't coordinate? Why shouldn't we include a housing subsidy as part of a welfare payment, if you will, that really does focus everything on the individual and allows the individual to make the determination about what is in their best interest?

Mr. UTT. Because I think, for the most part, housing policy over the last 20 years has been made more by the intermediaries in the housing assistance industry, such as the public housing authorities, the nonprofits, developers. I think the reason for that is over the last 20 to 25 years housing policy in this country has not been made with the direct input of the tenants or the beneficiaries in this, but rather with the input of the intermediaries in the housing assistance program. This includes the public housing authorities, nonprofit developers, private sector developers, financiers, tax lawyers—all of whom have benefited mightily from the project-based assistance that has been the predominant form of housing assistance.

We knew everything we knew about problems with project-based assistance and efficiency of the voucher program in the early 1970's after the experiments were conducted. The reason for those experiments was dissatisfaction with public housing and project-based assistance.

The things that Senator Kerry was saying about inefficiencies and mismanagement were the things that we were saying at HUD when we were dealing with the then scandals, and we have gone through subsequent waves. It is a system that defies reform. It is a system that defies efficiency and improvement.

You can have inefficient managers only if you have monopoly managers who have clients who have no choice. The people in public housing projects or subsidized projects have no choice. They are on a waiting list. It is not an entitlement. It is a first-come, first-served basis. You take what is given to you. And if you leave that project because you are dissatisfied, you have no place to go.

That kind of monopoly attitude perpetuates the kind of mismanagement that you see. If you give assistance to the individual tenant, they can exercise their right. If they are not satisfied with the management, they leave.

Senator MACK. I'll let you respond here in just a minute, Mr. Downs.

But I think what I was getting at, more specifically, was: you're talking about consolidating both welfare assistance——

Mr. UTT. Yes.

Senator MACK [continuing]. As defined today, and the housing assistance into kind of one subsidy.

Mr. UTT. Provided by one entity rather than the four different entities that provide the basic welfare system today, which is not very efficient, not very effective, and not very suitable for a new welfare system that is designed to move people off of welfare rather than perform rather inefficient, costly custodial function.

Senator MACK. You wanted to respond, Mr. Downs?

Mr. DOWNS. I agree that there should be some kind of coordination between housing assistance and welfare assistance, because for most households who receive housing assistance, it is essentially an increase in their incomes that doesn't improve the quality of their housing.

But the welfare programs of the country that already distribute housing assistance to millions of households have no quality constraint on the housing units they occupy. Therefore——

Senator MACK. Let me interrupt you there for a second, because the implication there is that the State or Federal Government ought to be doing something to make sure that individual who has got some flexibility lives in a unit that is in better condition than what they are presently living in, and we're making the same argument on the other side that we've actually got in place policies that force people to stay in project-based——

Mr. DOWNS. But that is the Congressional policy adopted in the Housing Act of 1949—that Congress wants to have every American living in a safe, decent, sanitary dwelling.

Senator MACK. But what I'm saying is that there is a—I don't argue with that. What I'm saying is you are already having that existing today in what people consider to be deplorable conditions. There are some places where we are literally forcing—a tenant, because it is project-based assistance, in essence can't move.

Mr. DOWNS. I'm not trying to defend project-based assistance versus vouchers.

Senator MACK. OK.

Mr. DOWNS. I prefer vouchers myself. But HUD's voucher does have with it a requirement that it be used in a standard quality dwelling unit. That requirement is not present in welfare programs. If you combine all housing assistance with a large social welfare block grant, since States today do not enforce any housing

quality standards on the use of their money in welfare programs, why would they start doing so in the future?

Senator MACK. So you were suggesting that if we were to, as Mr. Utt has pointed out that we put some requirement like that——

Mr. DOWNS. I think if you don't require quality standards you are going to subsidize a tremendous number of substandard units just as the welfare programs in the country do today.

Senator MACK. I see we have piqued Mr. Weicher's interest.

Mr. WEICHER. Just briefly. Communities, cities do have housing codes. It becomes a question of enforcement whether or not cities are prepared to enforce the housing codes to make sure that welfare recipients and other people are living in decent housing.

Tony is suggesting that they are not doing that now and they are not going to do that and you need a quality standard enforced by the public housing authority or by another Government agency as part of the housing voucher/certificate program.

I think that probably it is correct that localities don't enforce their housing codes very vigorously. They enforce them when people complain, and perhaps not always then. It depends on the circumstance. But I think you can also set a housing quality standard that is high enough that you can't make a program work. You need to be careful about the housing quality standard that you establish in any program.

Senator MACK. I only have one more question to raise. Are there any cases in which retaining public housing would be cheaper than providing tenant-based assistance, particularly in well-managed developments?

Mr. WEICHER. There probably are. I think, though, that the situation—if you give the tenant the opportunity to move out of those projects with the voucher, the tenant is not likely to move out. The tenant is well-housed. The tenant is given the opportunity to stay put.

We're not talking in any of this about abandoning projects. We're talking about giving choice to residents as to where they want to live. In a well-managed project, those residents are quite likely to stay put.

If you are concerned that the PHA is getting a windfall out of it, one way to address that is to have what we used to have in some of the subsidy programs called a "shopping incentive." The tenant can negotiate a lower rent with the PHA, and the tenant can keep part of the difference and the other part of the difference goes back to the Federal Government.

Senator MACK. Mr. Utt.

Mr. UTT. I believe that is the preferred way to do it. I think that vouchers are——

Senator MACK. Let me state the question again. Is it a question of whether—can well-run public housing communities provide housing cheaper than a voucher?

Mr. UTT. I think in principle and in practice they can because many of these projects were built at a much lower cost at an earlier time. They don't pay any taxes, property or Federal. In principle, they can. I think that, at the same time, to keep those managers on notice, I would still provide the assistance through the tenant by way of vouchers and allow them to decide whether to stay there.

I think, again, the whole problem with poor management is that they are not answerable to their clients, to their tenants. To the greatest extent that you can empower the tenants, you put the management on notice that we have to perform on a day-to-day basis. Just because an existing management group is efficient today is no assurance that 5 years from now that will be the case.

Senator MACK. Did you want to comment on this?

Mr. DOWNS. Among the people that live in public housing, 35 percent are elderly. A lot of these elderly units have the characteristics we just described. They were built quite some time ago, but many of them are very well-managed. They could probably provide housing at a lower cost than a voucher or certificate. But I'm not saying that certificates wouldn't provide an incentive to management to do better, but there probably are quite a few existing units, especially those for the elderly, that could meet your criteria.

Senator MACK. Senator Faircloth.

Senator FAIRCLOTH. I think, if I understood Mr. Downs correctly, we're talking about the wrong problem. I have contended that for some time.

You said, if I understood you, the quality of people, the type of people that now were in public housing was the thing that had devalued the quality of the neighborhood and somewhat created the problem. In other words, that if the same people that had been there in—if the structure and character of the people hadn't changed, public housing projects would have been a great success, would have been better.

Mr. DOWNS. Yes, sir. I believe that.

Senator FAIRCLOTH. But they changed. The single parents and the structure of the people created the problem. Is that what you said?

Mr. DOWNS. Yes, sir. That's what I said.

Senator FAIRCLOTH. All right. That's what I wanted to know.

In the late 1930's something like—records were not that good, unfortunately—maybe 1 out of 15 children born in this Nation were born out of wedlock. Maybe even 1 out of 20. It was a very low percentage. Today it is roughly 1 out of 3 and rising rapidly.

We have spent, more or less, in the last 30 to 35 years, since the inception of poverty programs and welfare, when we really hit it big time, close to $5 trillion—$4.8 trillion or $4.6, pick a figure—on so-called "poverty programs." You just said it. The public housing has just—many projects are just destroyed by these people. Maybe the whole answer is welfare reform.

I have a welfare bill that would deny housing assistance to single, unwed teenage fathers, and yet some say this is a very harsh thing. Is it possible that we have encouraged, perpetrated by the entire welfare concept, created a problem with which we are now tinkering with public housing?

As you said, the character of the people changed. In other words, the neighborhood changed. It wasn't the buildings, the concrete, the mortar, and the bathrooms that changed, but by the welfare programs, by the housing projects, we changed the nature of the people.

Maybe we should just simply reverse and go back to where we were. What do you say to that, and what does the Brookings Institute say?

Mr. DOWNS. I can't speak for the Brookings Institution.

Senator FAIRCLOTH. But you are.

Mr. DOWNS. No, I'm not. I'm speaking only for myself. I can't speak for the Brookings Institution.

When I say the character of the people changed, I mean two things. One is the kind of change you are talking about—a change in the behavior of the population generally, such as the rise in broken families, etc. The other is the concentration of broken families in these public housing projects.

Senator FAIRCLOTH. Why did the character of the family change? Was it because they were thrust into the housing project?

Mr. DOWNS. No. I don't think so. I don't think that was the reason.

Senator FAIRCLOTH. Well why did the character of the family change? Without welfare, would it have changed? It changed when we went into the massive welfare programs. Would it have changed without them?

Mr. DOWNS. Yes, but not to the same degree. I think that welfare——

Senator FAIRCLOTH. You mean we'd have less illegitimacy and out-of-wedlock births if we hadn't had welfare?

Mr. DOWNS. To some degree yes, sir. I believe welfare programs are partly responsible, but only partly.

Senator FAIRCLOTH. That's a pretty good reason for getting rid of a lot of welfare then, isn't it?

Mr. DOWNS. No. Not necessarily.

Senator FAIRCLOTH. We should increase welfare so we'll have more illegitimacy?

Mr. DOWNS. No, but you might change the nature of the welfare instead of getting rid of it. I think there are other options besides all or nothing at all.

I think that the welfare system is only one of the contributing factors to the change in behavior patterns in the population. There are many other causes, such as the general shift in the moral responsibility of our culture as we emphasize——

Senator FAIRCLOTH. What caused it to shift in the moral—was that because of easy money and welfare?

Mr. DOWNS. No.

Senator FAIRCLOTH. What caused that?

Mr. DOWNS. A general shift in western civilization toward more self-indulgence and greater emphasis on individual achievement and self-development rather than on community responsibility.

Senator FAIRCLOTH. You don't think that $5 trillion borrowing by the country and putting it into these programs contributed to that?

Mr. DOWNS. It contributed, but it wasn't the cause. It certainly was not the only cause.

Senator FAIRCLOTH. What was the cause specific?

Mr. DOWNS. There isn't just one cause, Senator. It is an overall cultural movement that has been going on for a century.

Senator FAIRCLOTH. I firmly believe the $5 trillion was a major contributor.

Thank you, Mr. Chairman.

Senator MACK. Let me just ask one more question of Mr. Utt, if I could.

You had proposed encouraging States to allow tenants greater control over management and ownership of the Government-owned units in which they live. How would you propose encouraging States to implement these policies without micro-managing at the Federal level?

Mr. UTT. I think the issue to establish tenant ownership or management needs some encouragement and some assistance from the outside. I don't know that that needs to come from the Federal Government. That can easily come from the State and local governments or from the local public housing authority.

Senator MACK. I think I was thinking more in the sense of how would you make sure States moved in that direction without micro managing?

Mr. UTT. I would give the tenants that get vouchers in public housing projects more than one choice. The choice we are talking about so far or the choice in the HUD budget of this year was to either use your voucher to stay or leave. I think some additional choices would be to use your voucher to hire your own management or use your voucher to acquire the project in some basis, but you empower these people with the voucher to make their choices.

I think tenant management and tenant ownership are opportunities that should not be foreclosed. They shouldn't be forced on everybody, but everybody should have that as 1 of 4 or 5 opportunities to use with their voucher in a public housing project if the environment is suitable and if the interest is there.

Senator MACK. So you are suggesting that tenants could take their vouchers collectively or individually and empower themselves to purchase facilities that they live in?

Mr. UTT. And say to the public housing authority:

> Thank you very much for your assistance in the past, but we'd like to try someone new, and we'd like to be involved in the management. If you can come up with more flexible terms, we'd be delighted to work with you; otherwise, we can talk to some of the private sector management companies that are around town.

Now, there is an awful lot of interest on the part of tenants for that. I was talking to someone at HUD and——

Senator MACK. How do you deal with the issue of—I guess the technical issue—who owns the property?

Mr. UTT. The property is owned by the local public housing authority. Public housing projects are not owned by the Federal Government. I believe that there is clear title there——

Senator MACK. That's right.

Mr. UTT [continuing]. And the clear title belongs to the local public housing authority, which are entities created by their States and answerable to their State law. So I think within any State, if we are going to provide this option, we ought to make sure that the legal mechanisms are as tidy and clear as possible to allow people to pursue this opportunity if they wish.

Senator MACK. Are you familiar with how many tenant management organizations are out there and how many are moving in that direction?

Mr. UTT. John might be a better person to provide that number. I can probably get the number for you, because HUD tabulates that.

But I would like to say that HUD has 100 requests in this year for tenant ownership from different public housing projects that are also supported by their public housing authority. But HUD has the resources only to accommodate 11 as a consequence of past budget cuts and rescissions.

Senator MACK. Say that again. I'm sorry. I didn't understand you.

Mr. UTT. They have requests—bona fide requests—from about 100 tenant organizations that are supported by their local public housing authority—that is, both the tenants and the public housing authority would like to move to tenant ownership. They have submitted formal requests to HUD for assistance. HUD has the resources this year to only accommodate 11 of those groups.

Senator MACK. Thank you.

Mr. WEICHER. Thank you, Senator. This is one of the programs which we put in place in the last Administration, as you know, the opportunity for residents to own their own public housing communities. Unfortunately, in this Administration it has been badly scaled back on the grounds of cost, which I think is incorrect as a factual statement of the problem.

But in a study which we commissioned and which we produced just before the end of the Administration, we looked at 80 resident management groups around the country which were far enough along to begin the process of managing their project if they wanted to, and in another study we looked at a dozen which had already taken over management and in some cases ownership.

Beyond that, the number that comes to my mind is that there were 300 other tenant groups which had been established in this very recent period under the impetus of the program that we had put in place between 1989 and 1992. And those organizations were starting the process of at least seeing if they wanted to manage or buy the developments that they live in.

I think you can establish through those organizations the opportunity for residents to own their housing as a cooperative, as a condominium, and if a significant fraction, a significant majority of the residents want to own the development they now live in, then you can build that into the program where you would voucher out the public housing.

I think some residents undoubtedly would want to. Other residents would not. That's fine.

Senator MACK. Again, I thank all of your for your testimony today. In my effort to try to do an hour per panel—well, we missed it by about 40 minutes.

Thank you very much for being here.

Hearing adjourned.

[Whereupon, at 12:40 p.m. the Subcommittees were adjourned, to reconvene at the call of their respective Chairs.]

[Prepared statements and additional material supplied for the Record follow:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

I want to thank Chairman Mack and Chairman Faircloth for holding this important hearing on the mission and future of HUD. This is a critical hearing that will help establish a framework for addressing HUD's many problems and future responsibilities.

The new Congress represents a tremendous opportunity to shed Federal micromanagement and the current "one size fits all mentality" that plagues many Federal programs and, in particular, plagues Federal housing and community development programs; it is time to redirect housing and community development decisionmaking back to State and local level.

Nevertheless, despite this tremendous opportunity, I also emphasize that a number of our choices, for good or ill, will be dictated by growing requirements of limited budget choices and fiscal responsibility; the Federal Government cannot keep writing checks for our current discretionary spending with the expectation that our children and future generations should pay for existing program decisions, no matter how wise or foolish.

As most of you know, I have pledged to begin addressing HUD's many budgetary problems as Chairman of the Senate VA/HUD Appropriations Subcommittee. Moreover, I look forward to working with Chairman Mack, as well as Chairman D'Amato and Chairman Faircloth and the other Member of these Subcommittees to find legislative solutions to many issues facing HUD and its programs. I think the Housing Opportunity Subcommittee has a historic opportunity to report out legislation that will fulfill the promise of our recent election and place the primary responsibility for housing and community development decisions squarely in the hands of States and localities.

This brings me to the Department of Housing and Urban Development. HUD is a dysfunctional agency that requires a complete reevaluation of its mission and a major reform of its programs and program operations. For example, the Department has grown from an agency responsible for 50 programs in 1980 to an agency that currently administers some 240 programs.

This is unacceptable. HUD does not have the capacity to administer all these programs and the mounds of regulations which now come with these programs. I want to emphasize how discredited HUD has become in the eyes of Congress and the American people; even Senator Dole has indicated that HUD should be considered for elimination.

Nevertheless, unlike some of my colleagues, I believe that total elimination of HUD will be difficult because of HUD's many long-term financial commitments and obligations. I also believe some Federal presence is necessary to ensure that certain basic housing and community development needs are addressed. In addition, we do not want to pass our unpaid housing and community development obligations onto States and localities.

The President's Budget for FY 1996 offers little in the way of concrete solutions to the fiscal, program, and organizational problems facing the Department. At best, the President's Budget suggests increases in the HUD Budget of some $20 billion in Budget Authority and $14 billion in Outlays over the next 5 years and then gives lip-service to reform through block grants proposals which are little more than extensions of current programs and which will be micromanaged at the Federal level through what HUD calls "performance-based goals." In fact, CBO has indicated that the President's Budget has underestimated the cost of HUD housing and community development assistance by some $27 billion over the next 5 years.

It is clear, however, that this Congress wants to change HUD and that reform must take place. As we think about the responsible reform of HUD, I think that it is useful to set some simple principles to guide our decisionmaking. I would like to propose four basic pillars of change for HUD that I offer for your consideration:

1. Any reform should be designed to provide protection for the tenants who depend on HUD for the roof over their heads;
2. Any reform should try to protect and maintain the good affordable housing stock of the Nation, while allowing obsolete and unusable housing to be demolished and replaced, where practical and according to local needs;
3. Any reform must consolidate most of the 240 existing HUD programs into fewer programs that accomplish HUD's mission and which generally defer to State and local decisionmaking; and
4. Any reform needs to presume that State and localities are our partners in addressing the housing and community development needs of our communities, and that we should provide the maximum flexibility possible to those States and communities that administer housing and community development programs responsibly.

From this foundation, I suggest that we rebuild HUD through the development of three basic block grants, keeping three of its targeted programs, and by moving some functions out of HUD altogether:

1. A *Public Housing Block Grant* which consolidates all current public housing programs. Funding would be allocated to all PHA's, with maximum entrepreneurial flexibility for PHA's to customize their activities to meet their local community needs. Poorly run PHA's would have to submit action plans to HUD for approval, and troubled PHA would be subject to receivership. I stress flexibility for PHA's to create better income mixes, reward employment, and to tear down obsolete housing at the discretion of the community.

2. An *Assisted Housing Block Grant,* with Section 8 funding provided directly to States. States would have broad latitude to design programs, and could, for example, authorize their State housing finance agencies and/or PHA's to administer the Section 8 programs.

3. A *Community Development Block Grant* which would consolidate, among others, the HOME program, the homeless assistance programs, and the existing CDBG program. Funding would be provided under existing CDBG funding formula, with, however, 40 percent of funding allocated to the States and 60 percent of funding allocated to entitlement communities; there would also be a 25 percent match requirement and a match waiver for distressed communities.

4. *Retain the Section 202 Elderly Housing program, the Section 811 Disabled Housing program, and the Housing Opportunities for Persons with AIDS program.* These are successful programs which meet the needs of special populations.

5. Conduct a top-to-bottom review of the *FHA mortgage insurance programs* to establish the mission and parameters of the individual FHA programs. HUD has failed to provide adequate data to justify a new corporate FHA, especially a new corporate, entrepreneurial FHA which would likely compete with the private sector.

6. Move the Office of Fair Housing and Equal Opportunity to the Department of Justice and the Office of Federal Housing Enterprise Oversight to the Treasury.

These proposals impress me as discussion points for remaking HUD. At every step, we need to treat our performing State and local partners as genuine partners, and grant them the greatest authority and flexibility possible in making program decisions. Nevertheless, we have the responsibility to *fix* the problems in our Federal housing and community development programs before we pass these responsibilities to States and local governments.

Again, thank you for having this hearing today. I very much look forward to working with you on the many difficult and complex issues facing HUD.

United States General Accounting Office

GAO

Testimony

Before the Subcommittees on Housing Opportunity and Community Development and HUD Oversight and Structure, Committee on Banking, Housing, and Urban Affairs United States Senate

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HOUSING AND URBAN DEVELOPMENT

Reform and Reinvention Issues

Statement of Judy A. England-Joseph,
Director, Housing and Community Development Issues,
Resources, Community, and Economic Development Division

GAO/T-RCED-95-129

Mr. Chairman and Members of the Subcommittee: We are pleased to be here today to help set the stage for addressing the budget and management problems facing the Department of Housing and Urban Development (HUD). HUD has severe organizational and management problems that it is still in the early stages of addressing. Because HUD's programs consist of large Federal loan commitments and discretionary spending, controlling the agency's spending will require the reexamination of Federal housing and community development policies and HUD's mission.

Our testimony today is based primarily on issued reports and testimony over the past 3 years (see app. IV). We will focus on (1) longstanding management deficiencies at HUD and its progress in addressing them, (2) problems that HUD and the Congress face in public and assisted housing programs—which account for the bulk of HUD's outlays, (3) the challenges that HUD faces in restructuring its programs and mechanisms for delivering them, and (4) fundamental questions that should be addressed in considering future housing and community development policies.

In summary:

- Four longstanding Department-wide deficiencies hamper HUD's ability to effectively carry out its mission and led us to designate HUD as a "high-risk area." These deficiencies are weak internal controls, an ineffective organizational structure, an insufficient mix of staff with the proper skills, and inadequate information and financial management systems. In a report issued last month, along with reports on the other 17 high-risk areas that we have tracked over the past few years, we point out that HUD's top management has focused much attention and energy on addressing these deficiencies.[1] However, many of these efforts are still in their early stages, and HUD has a long way to go.
- HUD and the Congress have a particularly vexing set of problems to deal with in the area of public and assisted housing. These problems include how to (1) minimize the $10 billion in mortgage loan defaults HUD expects over the next 6 years and address the physical inadequacies of insured multifamily properties; (2) deal with billions of dollars of backlogged housing rehabilitation needs, increased vacancy levels, and declining tenant incomes that exist in public housing; and (3) address the spiraling costs of providing housing subsidies to lower-income families.
- To address these and other problems, HUD has recently proposed a major change in its programs and program delivery mechanisms through its Reinvention Blueprint. If the Congress supports HUD's reinvention strategy, implementing it will require major legislative overhauls and revisions to HUD's regulations. It will also place more responsibility on the States and localities to develop new plans to implement programs and to develop performance: measures. Considerable effort will also be needed to transform the Federal Housing Administration (FHA) as envisioned in the Blueprint.

Solving the problems at HUD and deciding whether to adopt the agency's Reinvention Blueprint or alternatives to it will be difficult and will require reexamining Federal housing and community development policies and HUD's mission. Questions that must be addressed include (1) what policies best meet the needs of the people HUD serves, including the poor and those living in distressed communities, (2) how should these policies be implemented, and (3) what levels of Government should deliver program services? Reforms—be they mild or drastic—could have serious budget and social implications because HUD currently serves millions of Americans by providing rental subsidies, making home ownership more accessible, addressing housing discrimination, and helping revitalize communities.

HUD's Programs and Budget

Established in 1965, HUD is the principal Federal agency responsible for programs dealing with housing and community development and fair housing opportunities. Among other things, HUD's programs provide (1) mortgage insurance to help families become homeowners and to help provide affordable multifamily rental housing for low- and moderate-income families, (2) rental subsidies for lower-income families and individuals, and (3) grants and loans to States and communities for community development and neighborhood revitalization activities.

HUD's fiscal year 1996 budget proposal requests about $26 billion in budget authority and plans about the same level of outlays. Compared with fiscal year 1995 levels, this budget proposal represents about a 2-percent increase in budget authority and a 2-percent decrease in outlays.

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[1] *Department of Housing and Urban Development* (High Risk Series, GAO/HR-95-11, February 1995).

HUD's fiscal year 1996 budget summary projects savings of $51 billion in budget authority and $13 billion in outlays for fiscal years 1996 through 2000: These savings are based on a comparison with HUD's current services budget, which does not reflect the reinvention proposal and assumes, instead, that existing laws, regulations, and policies will remain in effect.[2] However, budget authority and outlays for fiscal years 1996 through 2000 are higher than would be needed if funding were frozen at the fiscal year 1995 level and no adjustments were made for inflation. Looked at this way, the budget request represents an increase in budget authority of about $21 billion and an increase in outlays of about $11 billion for the period 1996 through 2000. Appendixes I and II show comparisons of budget authority and outlay estimates for fiscal years 1996 through 2000.

HUD's Management Deficiencies

Scandals that occurred during the late 1980's focused public attention on management problems at HUD. Internal control weaknesses, such as a lack of necessary data and management processes, were a major factor leading to the HUD scandals. Organizational problems included overlapping and ill-defined responsibilities and authorities between HUD's headquarters and field organizations and a fundamental lack of management accountability and responsibility. An insufficient mix of staff with the proper skills has hampered the effective monitoring and oversight of HUD's programs and the timely updating of procedures. Poorly integrated, ineffective, and generally unreliable information and financial management systems have failed to meet program managers' needs and have not provided adequate oversight over housing and community development programs.

HUD's slow progress in correcting the fundamental management weaknesses that allowed such incidents to occur and a concern that HUD needed congressional attention led us to decide in January 1994 that the Department warranted the focused attention that comes with being designated by GAO as a high-risk area. Similar management deficiencies at HUD have been reported by HUD's Office of Inspector General (OIG) and by the National Academy of Public Administration (NAPA). In addition to pointing out problems with HUD's organization, staff capacity, and information management and systems integration, NAPA reported that HUD has, from its inception, struggled to find a coherent identity.[3] A primary reason for this struggle is the huge number of programs that HUD administers and the diversity of these programs. Between 1980 and 1992, the number of programs for which HUD had statutory responsibility increased from 54 to just over 200.

As noted in our February 1995, high-risk report on HUD, the agency's top management team has focused much attention and energy on addressing these deficiencies. HUD has formulated a new management approach and philosophy, intended to balance risks with results; has begun to implement a substantial reorganization of its field office structure; and has initiated a number of other actions that begin to address its four fundamental management deficiencies. However, the agency now faces the formidable challenges of completing its plans, translating its plans into effective actions, and implementing its new management approach into the fabric of the Department's day-to-day operations. Sustained focus, commitment, and diligence by HUD's leadership and staff will be needed—something that has not accompanied past attempts at reform and that was recently reported as a concern by HUD's Inspector General.

Examples of Major Budget and Management Problems

I would now like to discuss three areas that illustrate some of the budget and management challenges that face HUD: multifamily insured and assisted housing, public housing, and the high cost of public and assisted housing activities. Public and assisted housing activities account for over three-fourths of the agency's outlays for discretionary activities (see app. III).

HUD'S MULTIFAMILY HOUSING PORTFOLIO: STATUS AND PROBLEMS

HUD directly subsidizes and/or insures over 20,000 multifamily properties with about 2 million units. These properties expose the Federal Government to substantial current and future financial liabilities. Also, while much of this inventory reportedly is in decent condition, it has been estimated that at least 15 percent of the inventory has severe physical problems that threaten tenants' health and safety.

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[2] Current services budgets that reflect the anticipated costs of continuing Federal programs at present levels without policy or legislative changes are developed as part of the annual budget process.

[3] *Renewing HUD: A Long-Term Agenda for Effective Performance,* National Academy of Public Administration (July 1994).

A large portion of HUD's assisted housing liabilities derive from the use of FHA mortgage insurance, which protects lenders from financial losses stemming from borrowers' defaults. FHA insures about $43 billion worth of mortgage loans that support about 14,700 properties.[4] Many FHA-insured properties also receive other HUD assistance, such as below-market interest rates or Section 8 project-based rental assistance.[5]

A large number of defaults on FHA-insured loans have occurred in the past and are expected to continue, partly because FHA has not effectively managed its portfolio. In 1993, FHA paid out over $700 million in multifamily insurance claims. FHA has also estimated that it could lose $10.3 billion as a result of future defaults on loans in this portfolio. This amount would have been even higher without the prospect of continuing Section 8 project-based and other types of assistance used to prevent or delay loan defaults. While some loan defaults are inevitable, early identification of troubled loans and prompt actions to address underlying problems are essential if defaults are to be minimized. Numerous studies over the last two decades by Price Waterhouse, HUD's OIG, and GAO have identified weaknesses in HUD's default prevention activities. Many of the weaknesses identified were related to the fundamental department-wide deficiencies that we noted earlier in this statement.

Another critical problem facing HUD is that in many cases the cost to the Government of providing Section 8 project-based subsidies to assisted properties is excessive. For example, HUD has estimated that about three-fourths of the almost 10,000 Section 8 New Construction and Substantial Rehabilitation properties are subsidized at levels that are in excess of comparable market rents.[6] In some cases, the rent levels are as much as 75 percent higher than market rents. Furthermore, many multifamily properties for which HUD provides Section 8 assistance are in poor physical condition. A 1992 study estimated that about 3,200 HUD-assisted and/or insured properties were in such severe physical and financial condition that it would cost almost $1 billion to correct those problems. Some of these properties were the subject of hearings held last year at which both we and the HUD Inspector General testified.[7]

While HUD has various enforcement tools to ensure that owners maintain HUD-assisted properties in compliance with housing quality standards and other requirements, the agency has used these tools sparingly and inconsistently. Also, current legislation and regulations limit HUD's discretion in dealing with certain properties in its multifamily portfolio. For instance, the current legislation on property disposition generally requires that HUD preserve the housing so that it remains available to and affordable for lower-income households.

HUD has initiated actions to improve its ability to prevent default in multifamily properties, such as contracting out for property physical inspections and financial statement reviews and taking steps to develop an early warning system that should better identify financially troubled properties. Also, in November 1994 HUD organized a 24-member Special Workout Assistance Team to help field offices resolve the physical, financial, and ownership problems of troubled insured multifamily properties. Many of HUD's default prevention initiatives are in the early stages.

PUBLIC HOUSING: BUDGET AND MANAGEMENT ISSUES

Significant problems continue to plague public housing, adversely affecting many of the 1.4 million individuals and families who live there. While much of the public housing stock is in good condition, and is estimated to cost between $75 and $90 billion to replace, costly modernization needs have accrued and operating subsidy costs continue to mount. Despite the nearly $8 billion in modernization and operating funds provided annually by HUD, billions of dollars of backlogged needs for housing modernization, reduced rental income due to declining tenant incomes, and increased vacancy levels are problems that must be addressed.

Since 1981, almost $15 billion in modernization funding has been provided for public housing. Despite this funding, a backlog of at least $20 billion exists and needs continue to accrue. The backlog of modernization needs puts these properties

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[4] See also *Multifamily Housing: Status of HUD's Multifamily Loan Portfolio* (GAO/RCED-94-173FS, April 12, 1994).

[5] Project-based subsidies are attached to specific properties.

[6] The Section 8 New Construction and Substantial Rehabilitation programs provided assistance to private developers to construct new units or to substantially rehabilitate existing units for rental to low- and moderate-income families. About 4,500 of the 10,000 properties are also FHA-insured.

[7] *Federally Assisted Housing: Conditions of Some Properties Receiving Section 8 Project-Based Assistance Is Below Housing Quality Standards* (GAO/T-RCED-94-273, July 26, 1994) and *Federally Assisted Housing: Expanding HUD's Options for Dealing With Physically Distressed Properties* (GAO/T-RCED-95-38, October 6, 1994).

at risk of further deterioration and worsens the living conditions of affected public housing residents.

The second problem that public housing faces is that a shift over time from serving the working poor to serving the poorest of the poor has resulted in a need for increased operating subsidies. A decline in the incomes of public housing residents—the median annual income is now around $7,500—has resulted from changes in Federal laws that require public housing agencies to give higher priority for admission—called preferences—to the poorest of the poor. This, coupled with requirements that residents pay 30 percent of their income for rent has meant that the need for operating subsidies has increased. In the last 6 years, the costs of operating subsidies have increased by $1 billion, from $1.9 billion in 1990 to $2.9 billion in 1995 (both amounts in nominal dollars).

Increased vacancy levels have also had a detrimental effect on public housing. Vacant units provide no rent revenue, which leads to greater needs for operating subsidies from HUD. Also, a unit of vacant housing means that an income-eligible family on the waiting list is not receiving public housing assistance. Since 1984, the average vacancy rate has increased from 5.8 percent to 8 percent. However, in some large public housing agencies where there are uninhabitable buildings, vacancy rates range from 15 to 41 percent. In our ongoing survey of public housing agencies, we identified 1,177 totally vacant buildings. Vacant buildings also exact a high toll in drug-related crime and vandalism.

With demand in most cities exceeding supply, why are vacancy rates in public housing so high? One of the primary reasons has been the lack of an effective maintenance program; that is, a lack of preventive maintenance, an inability to spend modernization funds in a timely manner, and little accountability for maintenance at the housing project level. As it now stands, HUD's fiscal year 1996 budget request could add to this problem. HUD is proposing to fund 93 percent of the operating subsidies—down from 96 percent in fiscal year 1995—for which public housing agencies are eligible according to its funding formula. Since operating subsidies make up the difference between expenses—such as routine maintenance—and rental income, reducing subsidies may lead to more deferred maintenance.

The problems with public housing are also a result of HUD's inadequate oversight. Although the Congress has provided HUD with significant authority for overseeing and intervening in the management of a housing agency, many of the same agencies continue to be plagued with poor conditions and poor management. We are currently conducting work related to HUD's oversight of troubled public housing and will keep you informed of our progress.

HIGH COST OF PUBLIC AND ASSISTED HOUSING PROGRAMS

Since 1977, the number of families assisted by HUD's rental subsidy programs has increased by over 2 million.[8] The cumulative effect of this increase and the high cost of providing subsidies creates severe budget pressures on the Congress as it tries to meet deficit reduction goals.

According to the Congressional Budget Office (CBO),[9] both the number of families that receive rental assistance and the Federal outlays for those subsidies have increased almost every year since 1977. CBO reported that the number of assisted families almost doubled from 1977 through 1994, rising from about 2.4 million to about 4.7 million. Growth has been generally slow over the past few years because the Congress provided funds for fewer additional units. Outlays for rental assistance have also increased steadily since 1977. According to CBO, real outlays (adjusted for inflation) more than tripled from 1977 through 1994, rising from about $6.6 billion to about $22 billion (in 1994 dollars). Outlays are expected to remain at the same current high level, if not grow somewhat. The relatively rapid growth in outlays is primarily due to (1) increases in the number of assisted households and (2) rents that increased while the incomes of the clientele served declined.

What does the high cost of public and assisted housing programs mean for HUD? For one thing, without a major change in Federal housing policy, many of the housing programs have now reached the point at which they need additional budget authority to preserve the number and quality of the rental units that current pro-

[8] These programs include public housing, Section 8 tenant-based and project-based assistance, and Section 236 assistance (generally, subsidized interest payments to help produce rental housing).

[9] *The Challenges Facing Federal Rental Assistance Programs*, Congressional Budget Office (December 1994).

grams assist.[10] Budget authority needs are directly related to certain assumptions, such as the length of the term of the Section 8 contracts being renewed. Assuming a 5-year renewal period, CBO has estimated that the cost of preserving existing units will be, on average, about $22 billion in budget authority per year. As the Congress faces increasing pressure to reduce the deficit, these large amounts present difficult choices for policymakers who must consider competing needs.

HUD's Reinvention Blueprint

In December 1994, HUD introduced its Reinvention Blueprint. In the Blueprint, HUD proposes to address many of the management and budget problems facing it by restructuring and consolidating many of the agency's programs. The Blueprint envisions major changes in HUD's programs and organization, ending in three principal results: (1) removing public housing agencies from subsidy programs and making them compete with the private market; (2) consolidating 60 major categorical programs into 3 flexible, performance-based funds; and (3) establishing an entrepreneurial, Government-owned FHA. If the Congress supports HUD's reinvention strategy, implementing the Blueprint will require major legislative overhauls, revisions to the agency's regulations, and the design of formulas for allocating.funds that are now awarded competitively. It will also place more responsibility on States and localities to develop new plans to implement the programs and to develop performance measures. Considerable effort will also be needed to transform FHA as envisioned in the Blueprint.

REINVENTING PUBLIC HOUSING

Some of the most radical changes to existing programs are planned for the area of public housing. For example, under the Blueprint, public housing residents will receive portable rental certificates, wherever practicable, permitting them to seek better housing elsewhere. States, local jurisdictions, and neighborhoods would be given the flexibility to design public housing programs to meet their needs while, at the same time, the public housing stock would be forced to compete with other housing stock in the local area.

HUD sees this as beneficial because to be competitive housing agencies will have to improve the quality of their stock and seek a mix of tenant incomes, and because the agencies will be allowed to demolish buildings that are not cost-effective to rehabilitate. Furthermore, HUD has said that its proposal to give working families greater preference for admission to public housing will boost these families' efforts to achieve self-sufficiency by allowing them to keep more of their income when they get a job or get a raise. Also, by admitting tenants with higher incomes, HUD expects some reduction in the need for operating subsidies since rents will still be determined as a portion of income. However, HUD's reinvention of public housing will require major legislative and regulatory changes, including:

- Repealing the current requirement that housing agencies replace on a one-for-one basis any units they demolish or sell;
- Eliminating current Federal preference rules for admission to public housing that give the highest priority to admitting the poorest of the poor;
- Consolidating a variety of public housing capital programs into a single capital grant to housing agencies;
- Consolidating funding for anti-crime purposes, coordinating services, and providing operating subsidies for public housing into a single fund; and
- Requiring HUD to assume control over troubled public housing agencies.

Reaction to HUD's Blueprint by low-income advocacy groups and public housing agencies has not been wholly positive, however. Low-income housing advocates believe that tight rental markets and the potential for housing discrimination work against the success of relying on tenant-based, portable assistance. Moreover, vulnerable populations—such as the elderly—are not likely to have a desire to seek out alternative housing opportunities. And housing authorities fear that they will have to compete with privately owned rental housing without being granted regulatory relief and with the burden of some of their housing not being in shape to be marketable. Concerns have also been expressed that vouchering out portions of the public housing inventory is likely to have significant cost implications.

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[10] Budget authority would be needed for several purposes, including (1) extending the life of assistance contracts that have started to expire, (2) providing incentives to owners of certain assisted housing projects to prevent them from dropping out of Federal housing programs, (3) disposing of projects whose owners have defaulted on their federally insured mortgages, (4) continuing operating subsidies for public housing, and (5) reducing the accumulated backlog of repairs to the stock of assisted housing.

HUD is already finding out that its plans for converting all public housing to tenant-based assistance within 3 years are overly optimistic. Program officials now estimate that the transition will take at least 8 years. HUD believes the longer transition period is needed (1) in order to allow housing agencies to expend the over $9 billion of modernization and other funds the Congress has already budgeted for these programs, allowing housing agencies to become competitive with the private market, and (2) to prevent the loss of valuable housing stock which might take longer than 2 to 3 years to be made marketable and which residents and local governments agree should be preserved. HUD officials recognize that there is still a substantial backlog of modernization needs and that billions of dollars have been invested in much of this stock. If public housing subsidies were converted to tenant-based certificates before the properties became competitive, the properties would lose vital rental income, which may prevent them from remaining available as affordable low-income housing.

EFFORTS TO CONSOLIDATE PROGRAMS

HUD has proposed additional program consolidations that impact community development, housing, and homelessness assistance programs. For example, HUD plans to create a Community Opportunity Fund that largely builds on the Community Development Block Grant (CDBG) program and an Affordable Housing Fund that consolidates programs for housing production, rehabilitation, and home ownership. HUD believes that creating these funds will (1) give States and localities added flexibility in how they spend funds and (2) achieve accountability for results.

While community organizations we reviewed generally favored flexible funding, they were concerned about the potential impact of competing priorities at the local level and with performance measurement requirements.[11] Community development experts advocate a multifaceted, comprehensive approach to address the complex, interrelated problems in distressed urban areas. Flexible funding facilitates this approach. However, some community organizations were concerned that program consolidations could mean reduced funding for some efforts—particularly those to serve the homeless—because of competing local priorities. In addition, we found through our work that community development researchers have had difficulty in developing performance measures for revitalization efforts because communities' needs differ and some activities may not be quantifiable.

TRANSFORMING FHA

Considerable effort will also be needed to transform FHA into the entrepreneurial, Government-owned corporation envisioned in the Blueprint. According to the Blueprint, a new FHA corporation would be smaller and cost the taxpayer less. The new corporation would achieve this by relying increasingly on third-party partners to design products that meet market needs and obtaining a corporate authority that would provide FHA business-like flexibility in employment, contracting, and deployment of resources. Eventually, it is envisioned that the corporation would have a small, but highly-skilled staff.

Simply revising FHA's charter will, however, not transform it from "a slow-moving Government bureaucracy," as the Blueprint describes it, into a "Government-owned, streamlined, market-driven enterprise." In particular, FHA will need to overcome the long-term staffing, information system, and internal control weaknesses that have impaired its effectiveness. Accomplishing this will, at a minimum, require staffing and organizational changes, adjustments in FHA's products and product delivery mechanisms, re-engineering of FHA's processes and procedures, and disposition of some of its current assets. Such changes will take considerable time and effort.

Clearly one of the major issues in restructuring FHA is resolving the multifamily housing problems that I discussed earlier in my statement. A key effort proposed in the Blueprint to address these problems is converting project-based Section 8 subsidies to tenant-based subsidies. Section 8 subsidies would—after a transition period—no longer be directly attached to property units; instead landlords would receive Section 8 subsidies only when units are occupied by tenants holding Section 8 vouchers or certificates. For insured properties that have rents above those in the marketplace, HUD would accomplish this by restructuring the properties' debt through a process known as "marking-to-market." This action would allow HUD to reduce rents to levels reflecting the properties' true market value. According to the reinvention Blueprint, this restructuring would take place when the properties' cur-

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[11] *Community Development: Comprehensive Approaches Address Multiple Needs but Are Challenging to Implement* (GAO/RCED/HEHS-95-69, February 8, 1995).

rent Section 8 contracts expire (or earlier if legally permissible). Also, it would, in many cases, result in claims against FHA's insurance fund.[12]

HUD believes this approach would have various benefits, including lowering the cost of providing Section 8 assistance, increasing residents' ability to move to apartments of their own choice, reducing Federal support for substandard properties, and avoiding what FHA has termed "simplistic preserve at all costs strategies which have proven unaffordable and ineffective." However, various concerns have been raised about the marking-to-market approach. These include that the approach would be extremely staff-intensive and would require FHA to supplement its staff by obtaining considerable outside technical expertise. Furthermore, to carry out the process successfully, FHA would need to limit subsidies to the precise amount needed to keep the project operating while not giving owners a windfall profit—a very complex endeavor—and to administer the process in a way that minimizes any adverse impact on residents, owners, managers, investors, and lenders. Along these lines, Standard and Poors has already announced that it intends to examine the ratings for bonds backed by Section 8 properties in part because of concerns that rent restructuring could compromise owners' ability to meet debt service payments. Standard and Poors' reviews will include both FHA-insured Section 8 projects and projects that are not FHA-insured. Reviews of the uninsured projects involve approximately $745 million of local and $8.3 billion of State agency debt that, according to Standard and Poors, all relies to some degree on income streams from project-based Section 8 assistance.

Partly because of these concerns, alternatives to HUD's marking-to-market approach have been proposed. One approach would simply discontinue project-based subsidies when Section 8 contracts expire or come up for renewal without restructuring the properties' debt. Households living in units receiving project-based assistance would be provided with tenant-based assistance, and the formerly subsidized projects would be left to compete for tenants with other privately owned housing. While proponents of this approach recognize that the approach may cause some projects to go into default, they believe that the cost to the Government will still be less than continuing to provide project-based subsidies. HUD officials question this approach because they believe it would, among other things, provide a far less orderly transition to tenant-based assistance than the marking-to-market approach and is more likely to result in deterioration of the condition of properties that would, in turn, decrease property values and increase Federal costs.

Future Federal Housing and Community Development Policy

HUD's serious management and budget problems have greatly hampered effective implementation of its wide-ranging responsibilities. Major changes and actions are clearly needed. Such reforms, however, could have serious implications for the Federal budget, Federal agency management, and the families and institutions that HUD serves.

HUD's Reinvention Blueprint proposes a consolidation of many of the Department's programs. The Blueprint is an evolving document, and many of the details of how the restructuring would occur are still being developed. The Blueprint, however, envisions that HUD will retain much of its current mission, although the design and delivery of its programs will change. Others have suggested more drastic steps, such as moving HUD's functions to other Federal agencies.

Any proposal must recognize that HUD has massive financial responsibilities and administers programs that affect millions of people. Balancing business, budget, and social goals will be a formidable task. While each proposal will likely invoke considerable debate on its merits, we would like to lay out some fundamental questions that policymakers might ask in considering the Federal Government's role—and HUD's future—in housing and community development activities. The questions are as follows:

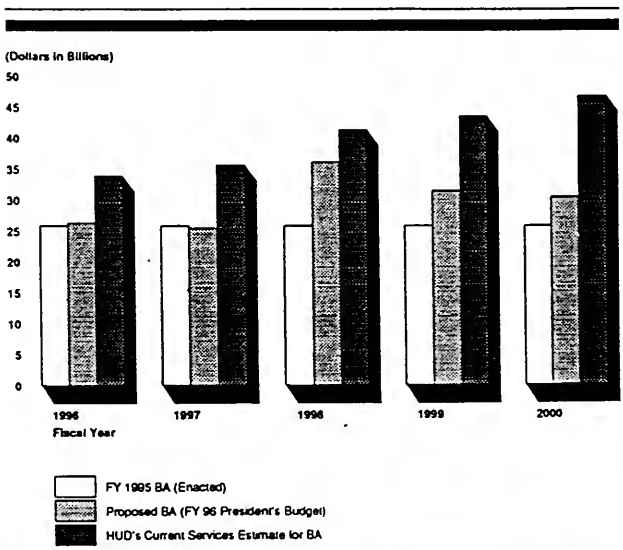
- What are the needs of the people HUD serves, including the poor and those living in distressed communities, and what Federal housing and community development policies can best meet these needs?
- How should Federal housing and community development policies be implemented? How should services be designed and delivered? How should funding be allocated? What mechanisms are needed to assure policymakers that funds are spent and populations are served as intended?

[12] Whenever feasible, the proposal calls for using "partial payments of claim" in which FHA would essentially reduce the outstanding mortgage on the property to the extent necessary for rents to be lowered to those reflecting the property's market value. The partial payment of claim would be captured in a "soft second mortgage" on the property that could be payable under certain conditions, for example, if the property is sold.

- What levels of Government should deliver programs and services? What is the capacity of those governmental entities to deliver the services? What actions, if any, are needed to enhance the capabilities of those entities to effectively implement their responsibilities?

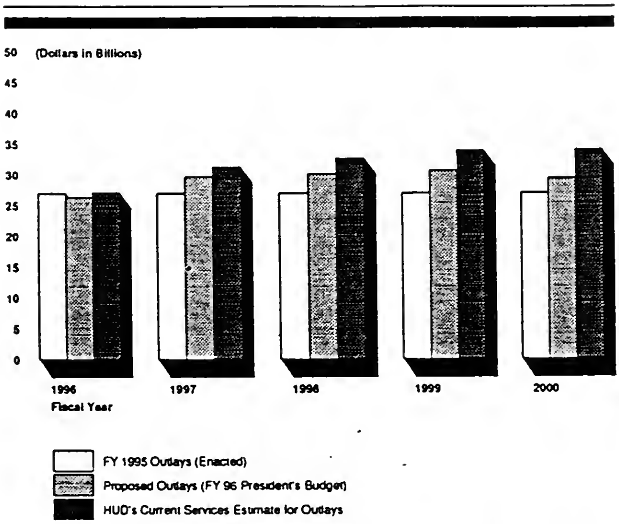
Mr. Chairman, this concludes our prepared remarks. We will be pleased to respond to any questions that you and other members of the Subcommittee might have. We in GAO look forward to working with the Congress to help address the issues before it.

A Comparison of Budget Authority for FY 1995, Proposed FY 1996, and Current Services Estimate



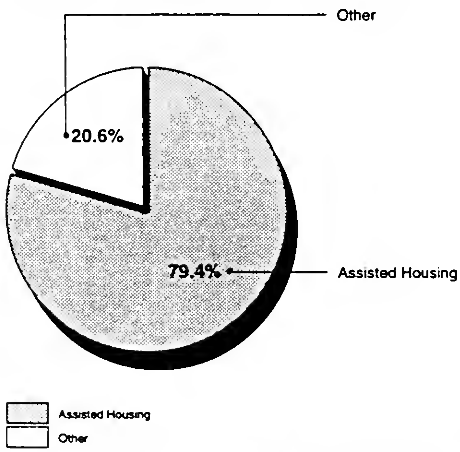
Current services budgets that reflect the anticipated costs of continuing federal programs at present levels without policy or legislative changes are developed as part of the annual budget process.

A Comparison of Outlays for FY 1995, Proposed FY 1996, and Current Services Estimate



Current services budgets that reflect the anticipated costs of continuing federal programs at present levels without policy or legislative changes are developed as part of the annual budget process.

HUD's FY 1996 Discretionary Budget Outlays (estimated)



The assisted housing category includes public and Indian housing and other housing programs. The other category includes community planning and development, the Government National Mortgage Association, Fair Housing, research, and administration.

Source: HUD's fiscal year 1996 Budget Summary.

SELECTED GAO PRODUCTS

Housing and Urban Development: Reforms at HUD and Issues for Its Future (GAO/T-RCED-95-108, Feb. 22, 1995).

Housing and Urban Development: Reinvention and Budget Issues (GAO/T-RCED-95-112, Feb. 22, 1995).

Department of Housing and Urban Development (High-Risk Series, GAO\HR-95-11, Feb. 1995).

Community Development: Comprehensive Approaches Address Multiple Needs but Are Challenging to Implement (GAO/RCED/HEHS-95-69, Feb. 8, 1995).

Housing and Urban Development: Major Management and Budget Issues (GAO/T-RCED-95-86, Jan. 19, 1995, and GAO/T-RCED-95-89, Jan. 24, 1995).

Federally Assisted Housing: Expanding HUD's Options for Dealing With Physically Distressed Properties (GAO/T-RCED-95-38, Oct. 6, 1994).

Federally Assisted Housing: Condition of Some Properties Receiving Section 8 Project-Based Assistance Is Below Housing Quality Standards (GAO/T-RCED-94-273, July 26, 1994, and Video GAO/RCED-94-01VR).

Public Housing: Information on Backlogged Modernization Funds (GAO/RCED-94-217FS, July 15, 1994).

Homelessness: McKinney Act Programs Provide Assistance but Are Not Designed to Be the Solution (GAO/RCED-94-37, May 31, 1994).

Section 8 Rental Housing: Merging Assistance Programs Has Benefits but Raises Implementation Issues (GAO/RCED-94-85, May 27, 1994).

HUD Information Resources: Strategic Focus and Improved Management Controls Needed (GAO/AIMD-94-34, Apr. 14, 1994).

Multifamily Housing: Status of HUD's Multifamily Loan Portfolios (GAO/RCED-94-173FS, Apr. 12, 1994).

Community Development: Block Grant Economic Development Activities Reflect Local Priorities (GAO/RCED-94-108, Feb. 17, 1994).

Housing Finance: Expanding Capital for Affordable Multifamily Housing (GAO/RCED-94-3, Oct. 27, 1993).

Assisted Housing: Evening Out the Growth of the Section 8 Program's Funding Needs (GAO/RCED-93-54, Aug. 5, 1993).

Multifamily Housing: Impediments to Disposition of Properties Owned By the Department of Housing and Urban Development (GAO/T-RCED-93-37, May 12, 1993).

HUD Reforms: Progress Made Since the HUD Scandals but Much Work Remains (GAO/RCED-92-46, Jan. 31, 1992).

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PREPARED STATEMENT OF SUSAN GAFFNEY

INSPECTOR GENERAL, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC

MARCH 14, 1995

While HUD suffers from many problems, it also does a relatively good job of administering some major housing and community development programs. The Office of Inspector General (OIG) does not believe, however, that this debate about HUD issues should initially focus on the viability of HUD as an organizational entity. We need instead to start by seeking a clear definition of the Federal Government's mission in housing and community development in this country, as well as a definition of programs and activities that support that mission.

The OIG believes that Secretary Cisneros' "Reinvention Blueprint" is a bold step in the right direction. Nonetheless, some cautions are in order: The Blueprint is lacking in the specificity needed for its full evaluation; parts of the Blueprint raise huge policy issues, while other parts are relatively straightforward and non-controversial; deficiencies in HUD management and administrative systems can be expected to hinder implementation of the Blueprint; and the relationship between announced cuts in HUD staffing and the steps outlined in the Blueprint is totally undefined.

While the Congress is debating the very significant issues raised by the Reinvention Blueprint, the OIG suggests that the Congress consider interim legislative action to reduce waste associated with HUD programs. Our many suggestions include the following.

- With respect to multifamily assisted housing: Elimination of the Loan Management Set Aside and Flexible Subsidy programs; elimination of statutory language that results in HUD's subsidizing rents far in excess of market rents; reform of the prepayment/preservation program; and reform of program enforcement and bankruptcy laws that serve to protect bad project owners.
- With respect to public housing: Repeal of the one-for-one replacement rule; repeal of statutory language that results in HUD's paying operating subsidies on long term vacant units; and revision of statutory provisions that unduly restrict public housing authorities in their rent and admission policies.

Even without any legislative action, HUD can and should—as a matter of great urgency—start moving to correct the most egregious problems affecting its programs. For instance:

- To make informed decisions on its portfolio of multifamily projects, HUD needs to obtain comprehensive physical, financial, and economic analyses of the projects as soon as possible.
- To deter gross mismanagement of insured/assisted multifamily properties, HUD needs to get tough and more aggressively use its existing enforcement tools.
- HUD needs to use its existing authorities to act aggressively and decisively in dealing with large troubled public housing agencies.
- HUD needs to immediately undertake a comprehensive assessment of the public housing stock, as a basis for determining the most cost effective and beneficial way of assisting developments now and in the future.

PREPARED STATEMENT OF JACQUELINE ROGERS

SENIOR FELLOW, UNIVERSITY OF MARYLAND, SCHOOL OF PUBLIC AFFAIRS
MEMBER, PANEL ON THE ORGANIZATION AND MANAGEMENT OF HUD
NATIONAL ACADEMY OF PUBLIC ADMINISTRATION, WASHINGTON, DC

MARCH 14, 1995

Mr. Chairman and Members of the Subcommittees: My name is Jacqueline Rogers, and I was a member of the panel on the Future Organization and Management of the Department of Housing and Urban Development (HUD) for the National Academy of Public Administration (NAPA).

The Academy is a private, nonprofit and nonpartisan organization chartered by Congress to improve the effectiveness of Government at all levels—Federal, State and local. Last year, pursuant to a congressional mandate, the panel completed a major study of HUD, including the Department's human resource requirements and management, financial management, systems integration, and resource estimation capabilities. The study's scope also included an assessment of HUD's organization.

The panel's final report, *Renewing HUD: A Long-Term Agenda for Effective Performance,* was issued in July 1994.

The Academy panel addressed the fundamental issues of how to simplify and consolidate programs and sustain management attention on building and maintaining HUD's institutional capacity. In doing so, we focused heavily on how the Federal Government can relate to communities in a more constructive manner. Copies of the panel's report have been provided to the Subcommittees, and I request that the Summary Report be included in the record of this hearing.

I am accompanied today by Al Kliman, who was the project coordinator and is known to many Members of this Committee in his former role of HUD budget officer, and Roger Sperry, the Academy's director of management studies.

The Challenge Ahead

After reviewing the evidence, our panel concluded that HUD is at a crossroads. It can become an effective public institution or it can continue down the now familiar road of poor performance. Our panel concluded that if, after 5 years, HUD is not operating under a clear legislative mandate and in an effective, accountable manner, the President and Congress should seriously consider dismantling the Department and moving its core programs elsewhere.

The NAPA panel made this statement because of underlying problems requiring further attention by both the Administration and Congress. This was not intended as an indictment of HUD's current leadership, whom we found to be both capable and qualified. In fact, we found that the current leadership was moving proactively on several fronts to resolve many of the management deficiencies described in our report, as well as reports by other organizations. What we said, however, is that there must be some basic changes in the underlying legislation. There must also be a management agenda agreed to by both the Congress and the Administration which would provide the continuity of effort to implement changes needed to finish the job of making HUD an effective institution of Government.

The Administration's reinvention proposal that Congress will soon have before it in legislative form will trigger the dialogue on comprehensive program reauthorization our panel was seeking. Two of the three key proposals are consistent with the panel's recommendations. The proposal to consolidate about 60 programs into three large block grants directly responds to our call for program consolidation. The proposal to convert the Federal Housing Administration (FHA) into a Government corporation is also responsive to another of our panel's recommendations. The proposals related to public and Indian housing were not considered by the panel.

The causes of HUD's underlying problems are not all found in one place. As the NAPA report sets forth, there was a lack of political consensus when Congress established HUD, and there is no consensus today on what is, or should be, the Department's mission. A part of the problem is what the report calls, an "expectations glut" where the rhetoric surrounding the Department—coming from both the Executive and Legislative branches—set up expectations far in excess of what HUD is authorized to do or could do with the resources it has available.

If HUD is to function effectively, the Administration, the Department, and Congress need to proceed expeditiously with a comprehensive reconsideration, consolidation and reauthorization of HUD's programs. Until the programmatic house is in order, no amount of tinkering with management will cure what ails this organization. Our panel recommended that HUD's program structure be consolidated into no more than 10 major programs. In the meantime, HUD should have additional waiver and demonstration authority to provide needed flexibility in meeting the varied needs of State and local governments and other housing providers.

Now that HUD has proposed to rationalize its program structure and make FHA a Government corporation, it is Congress' turn to act on a comprehensive reauthorization of the programs operated by HUD. We are concerned, however, that further reducing the staff of HUD in advance of program streamlining and consolidation could continue the mismatch between statutory requirements and available resources. We recommended that HUD develop a long-term management agenda to accompany reforms in its program agenda. A sensible and flexible legislative structure, program consolidation, management improvement and appropriate resource levels all are needed to make HUD an effective institution. This is what our panel was striving for.

I have attached a summary of the panel's major conclusions and recommendations which I request be included in the record, along with some information on the Academy and the panel which conducted this study.

Mr. Chairman, this concludes my prepared statement. We would be pleased to answer any questions you may have.

* * *

Attachment 1—Major Conclusions and Recommendations From the NAPA Report, *Renewing HUD, July 1994*

HUD in the Communities: Move from Requirements to Results

A consequence of having so many targeted and narrowly focused initiatives is that communities confront a confusing array of programs, each with their own application and reporting requirements. Communities are sometimes unable to allocate Federal resources on the basis of local priorities. Instead, to obtain HUD resources, States, localities, or other direct service providers must apply for more narrowly targeted funds often meeting a community's lower-priority needs, simply because those are the funds available.

Our panel recommended that HUD:

- Work through a single community planning mechanism to coordinate information and reporting requirements among HUD's programs and across its offices.
- Eliminate requests for data, in plans and reports, unless they are integral to direct program operations and HUD consistently uses the data.
- Emphasize the need to demonstrate results rather than to document processes. This must be done through substantive changes, such as modifying reporting requirements so that users are asked largely to present information on performance.
- Consolidate calls for data, among HUD's programs and across its divisions, and take advantage of technology. Automate data requests and input whenever possible.
- Work with Congress to draft amendments to the HUD Reform Act so that the Act's requirements, while working toward sound management and accountability, do not serve as impediments to HUD's goals in working with developers, direct service providers, and communities.

From Bit Player to Full Partner

While HUD's housing role in the Nation's communities has diminished, increasingly important parts have been played by State and local governments, other Federal departments, Government-Sponsored Enterprises (GSE's), private financial institutions, and innovative local lending programs. In many States, the housing finance agency is significantly more prominent than HUD in funding projects and in spearheading innovative programs. HUD's staff were not seen as having the sophisticated level of skills necessary to work on complex housing or community development issues, and HUD was not seen as creating incentives or providing the resources for its staff to become more meaningful partners with its communities of users.

"Partnership" has become a consistent theme at HUD in the mid-1990's, and there is commitment to this concept. It is not yet clear, however, where HUD will acquire the staff resources or flexibility to participate in the very time-intensive, sophisticated deal-making that is central to housing and community development partnering. True cross-program, community-based efforts are very labor intensive and cannot be done unless staff are trained to work cooperatively rather than as principally monitors or regulators. Still, commitment is the first step, and HUD has pledged to be a full partner with the Nation's communities.

Our panel recommended that HUD:

- Use the newly formed Community Empowerment Teams in HUD's 81 locations to seek regular input from HUD's communities of users on HUD policies and requirements and the impact they will have on communities.
- Minimize Washington-based interference in local decisions and partnerships.
- Legitimize interaction between HUD and the various communities it serves.
- Study the Negotiated investment Strategy concept, which entails intergovernmental negotiation to facilitate local urban strategies; consider implementing some of these concepts—without creating a separate program to do so.
- Revise the employee incentive system (expectations, rating criteria, and promotion considerations) to emphasize that working with communities and other agencies is as important as enforcing regulations.
- Undertake a major investment in retooling HUD staff to prepare for different kinds of relationships with all communities of users.
- Create short-term staff rotation assignments between HUD and State and local governments and nonprofit organizations.

HUD's Reorganization—More Changes Needed

In the new HUD organization, all authority moves along program lines and there is no local decisionmaker to integrate HUD's work in the communities. This is un-

likely to advance HUD's stated mission of creating communities of opportunity. As long as HUD's field structure is tied to the programs it administers rather than geared to helping communities leverage resources, it is not likely HUD will be an effective partner.

Our panel concluded that HUD should:

- Readdress the issue of providing field-level decisionmaking authority to area coordinators to work through inter-program issues among HUD staff and with communities;
- Take a hard look at how its new structure is meeting the Secretary's goal of putting communities first.
- Maintain a flexible attitude to change course as necessary.

Changes in workload and advances in communication technology mean that the HUD of the future will not need 81 offices scattered throughout the country. With processing centers handling location-neutral activities, HUD can function with a smaller number of full-service offices that have outreach programs joining in partnerships with communities. That does not mean that HUD needs to be a lesser player in the Nation's communities. HUD needs to be able to organize its work and allocate its staff to best fulfill its mission and to support intergovernmental and organizational partnerships that build on community priorities.

Our panel recommended that HUD:

- Maximize the use of processing centers to handle location-neutral activities.
- Use the next 2 years to determine the number of offices needed to effectively perform its mission and propose to Congress the needed workplace and workforce realignments.

Corporatize the Federal Housing Administration

The vertical program structure best serves a commercial-type function such as the Federal Housing Administration (FHA). FHA's insurance puts the Federal Government at substantial financial risk and requires a very different mode of operation to manage that risk properly. Thus, our panel recommended creating a separate structure for FHA within HUD. The FHA commissioner must be able to decide how to organize and manage this complex insurance enterprise in such a way that the Government's interest is protected over the long term. With the flexibility for administrative and product decisions, FHA will also be able to apply different program devices, depending on a community's needs, and can better work with the rest of HUD as a true partner in the Nation's communities.

Once FHA becomes a separate entity under the Secretary's policy direction, the Secretary can concentrate on creating a Department that ensures that issues are resolved in the HUD office closest to a community, and minimizes the number of problems that get bucked up to headquarters.

Management Systems and Initiatives

By any measure, our panel found HUD's management systems had failed to meet essential needs. They failed the Secretary in fulfilling his stewardship responsibilities to the American public. They failed to provide credible data for Congress on which to evaluate programs. And, not least, they failed HUD's staff on the front lines who need to be well-trained, highly motivated, and adequately served by computers and systems if they are to do their jobs well. Studies by HUD management, the HUD inspector general, GAO, congressional committees, and outside consultants all documented significant problems with HUD management systems. Secretary Cisneros recognized the inadequacies and placed a high priority on fixing the systems.

Overall, the panel concluded that HUD's initiatives were sound and moving in the right directions. Many of the problems in HUD's management systems, however, cannot be solved easily or quickly. Sustained efforts and concerted management attention—over a number of years and probably beyond the tenure of many of HUD's top leadership—is essential. Moreover, long-term commitment and support by HUD leadership, as well as the OMB (on behalf of the President), and by Congress are critical to the process.

Here are some observations on specific areas:

- **Financial management:** HUD has made a good start at addressing the Department's financial management problems. But, raising the quality of HUD financial management to an acceptable level *will take years of consistent and concerted leadership and effort.*
- **Information management:** HUD has moved aggressively to address its many problems in information management and systems integration. To build on these early successes, HUD needs to consider issues focusing on leadership and over-

sight, strategic business and information planning, information management, field involvement in systems, enterprise architecture, and investment in information infrastructure.
- **Staff estimation and allocation:** Any proposal for significant adjustments in HUD's resources—up or down—should be supported by an analysis of the impact of that adjustment on HUD's capacity to carry out its responsibilities.
- **Human resources management:** HUD's work force is not in good shape. It suffers from a poor public image and criticism from its clients, and it is aging. For nearly 15 years, HUD has done little to recruit new staff. Particular attention should be directed to staffing, executive and supervisory development, performance management, and staff communication.

Building and Maintaining the Institution: A Long-Term Agenda is Key

The policy and management initiatives of the Administration and Congress will have little value to the people to be served, and taxpayer dollars will continue to be at risk unless HUD creates a long-term institution-building agenda and a focal point to implement and track it. Here are the key elements:
- **Strong and sustained leadership for HUD** at headquarters and in the field.
- **An ensured supply of new staff talent.**
- **A focus for administration and management** that emphasizes continuity in leadership, systems, and organizational principles.
- **Change in culture** from reactive to proactive, from defensive to offensive.
- **Effective and stable core management systems** in information management, human resources management, and financial management.
- **A process for thinking and acting strategically** to ensure alignment between the Department's vision, values, goals, and legislative reforms.

Leadership Needed to Carry Out the Agenda

There are two key elements in providing the leadership for carrying out the long-term agenda. The first is clarification and consolidation of responsibility for developing and carrying out the agenda. The second is continuity. Sustained management competence and continuity are *vital* to building and maintaining an effective department. Without it, the discipline required to "stay the course" in rebuilding HUD will not be present. Our panel recommended that HUD:
- Develop legislation that would provide continuity of leadership by establishing an *under secretary for management* and requiring that the individual in this position be appointed by the President and subject to Senate confirmation with qualifications to manage a large public organization set forth in the law. Like the inspectors general, Congress should be notified on removal of any incumbent in this position.
- Assign responsibility for implementing elements of the agenda to specific individuals or groups under the leadership of the chief operating officer [deputy secretary], working with the under secretary for management.
- Provide a career staff to support the work of the under secretary.

The Challenge for Congress

The challenge for Congress is to help bring stability to the renewal of HUD and ensure predictability in its programs so that communities know what resources will be available. The 104th Congress should:
- Work with the Administration and the Secretary to develop a long-term agenda for change.
- Work with the Secretary in creating additional waiver and demonstration authority for HUD.
- Provide the continuous resource stream and support to keep the revitalization agenda on track.
- Hold annual hearings at which the HUD Secretary and leadership team report on their performance against the agreed-upon plan for rebuilding HUD as an effectively performing public institution.

Attachment 2—About the Academy

The National Academy of Public Administration is a nonprofit, nonpartisan, collegial organization chartered by Congress to improve governance at all levels—Federal, State, and local. NAPA works toward that end chiefly by using the individual and collective experiences of its Fellows to provide expert advice and counsel to Government leaders. Its congressional charter, signed by President Reagan in 1984, was the first granted to a research organization since President Lincoln signed the charter for the National Academy of Sciences in 1863.

The unique source of NAPA's expertise is its membership. It consists of more than 400 current and former Cabinet officers, Members of Congress, governors, mayors, legislators, jurists, business executives, public managers, and scholars who have been elected as Fellows because of their distinguished contributions to the Nation's public life.

Since its establishment in 1967, NAPA has responded to many requests for assistance from various agencies and has undertaken a growing number of studies on issues of particular interest to Congress.

Its work has covered a wide range of topics, including agriculture, education, health, human services, housing, urban development, prisons, courts, space, defense, environment, emergency management, human resources, organization and management analysis, and international public management.

ATTACHMENT 3—BIOGRAPHICAL SKETCHES OF THE NAPA PANEL AND PROJECT LEADERSHIP

Academy Panel

FEATHER O'CONNOR HOUSTOUN—Former Chief Financial Officer, Southeastern Pennsylvania Transportation Authority (SEPTA); Treasurer and Chief Financial Officer, State of New Jersey; Executive Director, New Jersey Housing and Mortgage Finance Agency; Deputy Assistant Secretary for Policy Development (Acting), U.S. Department of Housing and Urban Development.

ALAN L. DEAN—Consultant. Former Vice President for Administration, U.S. Railway Association; Deputy Assistant Director, U.S. Office of Management and Budget; Assistant Secretary for Administration, U.S. Department of Transportation; Associate Administrator for Administration, Federal Aviation Administration.

HENRY GARDNER—Senior Vice President, Donaldson, Lufkin & Jenrette, San Francisco, California. Former positions with Oakland City, California: Assistant Personnel Analyst; Administrative Assistant; Assistant to the City Manager; Assistant City Manager; City Manager.

JONATHAN B. HOWES—Secretary, Department of Environment, Health and Natural Resources, State of North Carolina. Former Research Professor and Director, Center for Urban and Regions Studies, University of North Carolina; Mayor, Town of Chapel Hill; Director, Urban Policy Center, Urban America, Inc.; Director, State and Local Planning Assistance, U.S. Department of Housing and Urban Development.

JOHN PARR—President, National Civic League. Adjunct Associate Professor, Graduate School of Public Affairs, and Former Director, Center for Public-Private Sector Cooperation, University of Colorado at Denver; Director, Colorado Front Range Project, Office of the Governor, State of Colorado; Special Assistant to the Governor, State of Colorado; and a licensed attorney.

JACQUELINE ROGERS—Secretary, Maryland Department of Housing and Community Development; 15 years with Montgomery County, Maryland, the last seven of which were as Director of the Office of Management and Budget; Faculty Member of the University of Maryland School of Public Affairs.

BARBARA SABOL—Consultant. Former Administrator/Commissioner, Human Resources Administration, City of New York; Executive Deputy Commissioner, Department of Social Services, State of New York; Secretary, Department of Health and Environment, State of Kansas; Director, Office of Policy and Planning, Department of Human Service, Washington, DC; Chief, Office of Program Coordination and Review, Office of Human Development Services, U.S. Department of Health and Human Services.

MITCHELL SVIRIDOFF—Professor, New School for Social Research, New York. Former President, Local Initiatives Support Corporation; Vice President, Division of National Affairs, The Ford Foundation; Administrator, Human Resources Administration, New York City; Executive Director, Community Development, New Haven, Connecticut.

JOEL D. VALDEZ—Vice President for Business Affairs, University of Arizona. Former City Manager, Assistant City Manager and Administrative Assistant, City of Tucson; Administrator, Detention Services, Juvenile Court, Pima County, Arizona.

Project Leadership

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HUD'S MISSION AND FUTURE

Thank you for inviting me to testify before the Subcommittees today. I am especially glad to be here because this year offers an opportunity to reconsider HUD's mission and redirect its programs. The Administration's "Reinvention Blueprint" for HUD opens the door for Congress to make major policy changes. The Blueprint is not in my judgment the ideal basis for reforming HUD. It builds on policy recommendations of past Republican Administrations, but: it contains bad ideas as well as good ones, and the changes are phased in very slowly. Nonetheless, it certainly changes the political landscape. Both taxpayers and participants in HUD programs could benefit if Congress takes this opportunity to reform HUD.

I should begin by stating that, although I am a Senior Fellow at the Hudson Institute, a nonprofit policy research institution, I do not speak for the Hudson Institute or any other group. I am here to speaks only for myself, based on my experience at HUD and my professional activities. I have served at HUD in three different Administrations over the last 20 years, most recently as Assistant Secretary for Policy Development and Research under President Bush and Secretary Kemp during 1989–93. Twice I came to HUD in the aftermath of scandals, in 1973 and in 1989. I am an economist by profession, specializing in housing and urban issues throughout my professional career.

In order to assess HUD's mission, it's useful to begin by considering what HUD does now: What it does well, what it does badly, and why. Then I'll discuss various reform options, including the Reinvention Blueprint.

What Does HUD Do Well?

(1) FHA single-family home mortgage insurance—Section 203—helps young, middle-income families buy homes and the insurance premiums cover the costs of foreclosure and claims. The Mutual Mortgage Insurance Fund has a positive net worth, and, thanks to reforms proposed by Secretary Kemp and President Bush and enacted by Congress in 1990, the Fund is moving toward an actuarially sound status. At present over 5 million homeowners have FHA insurance, and about 800,000 more buy homes with FHA-insured mortgages every year.

(2) HUD provides tenant-based housing assistance for over 1.1 million low-income families and individuals in its voucher and certificate programs. We now have 20 years of experience with vouchers and certificates, first as an experiment and then as a full-fledged program. They serve all kinds of families, in all kinds of markets. Over half of the families in the program are African-American or Hispanic. On a scale of 1 to 10, over two-thirds of recipients (including minority households) give their housing at least an 8. HUD operates the program effectively with a small staff.

(3) The Community Development Block Grant provides money for neighborhood revitalization to State and local governments. Half the money is supposed to be spent in low-income neighborhoods or for low-income people. The most common use of funds is for neighborhood improvements in housing, typically rehabilitation. (CDBG cannot be used to build new housing.) Money also goes for neighborhood facilities. Occasionally some use of funds becomes controversial; Indian reservations are able to use CDBG to develop gambling casinos, for example. But in general the program appears to support neighborhood housing and economic development activities reasonably effectively.

Each of these programs supports one of the major missions of HUD: To promote home ownership; to provide decent housing for the poor; to help maintain and improve the neighborhoods that Americans live in.

What Does HUD Do Badly?

(1) FHA's multifamily insurance programs don't work well and they don't cover their costs. Mortgages on multifamily projects are difficult to underwrite, and not just for FHA. Freddie Mac lost money on its multifamily mortgage purchases in the late 1980's and discontinued its multifamily programs for several years. Every multifamily project is unique, and has to be analyzed carefully, which is very staff-intensive. HUD has about eight times as much single-family mortgage insurance in force as multifamily insurance. However, HUD's staff is split about 52–48 between single-family and multifamily. Multifamily insurance takes a vastly disproportionate share of staff time and resources, including the central management of the department.

Even then the programs lose money. They require annual appropriations to cover losses. FHA has had to establish a $10 billion loss reserve against a portfolio of $44 billion. The losses are continuing: The budget includes a 7 percent subsidy rate for multifamily insurance on average, meaning that losses will be 7 cents on every dollar of multifamily insurance—in addition to the 5 percent insurance premium. Losses are projected to range from 2 cents to 27 cents in various multifamily programs. (A few small programs are expected to cover their losses out of premiums.)

Also, because multifamily insurance is difficult to do well, it's prone to abuse. There have been scandals in FHA multifamily insurance going back to the Section 608 program in the 1940's. They typically involve fraudulent underwriting: Inflating the estimated project costs so that well-connected developers are able to obtain insurance for more than the value of the project and avoid committing any money of their own.

(2) The problems with multifamily insurance are compounded in the privately-owned subsidized projects—the "insured assisted inventory." There is always pressure to underwrite these projects generously, "to make the program work." Then the project needs generous subsidies to support the mortgage. If the project still gets into financial difficulties, and many do, HUD makes great efforts to avoid foreclosure. That would be admitting failure, and would require HUD to manage it, something HUD does not want to do. The alternative is to put more money into the project. This has led to programs such as "Flexible Subsidy.

Scandals are especially likely to occur where subsidies are piled on top of each other. It's hard to limit the additional subsidies to exactly the amount that is needed to keep the project operating and not give the owners a windfall profit. If the subsidies are excessive, then they become valuable to the project owners. Well-connected consultants begin to lobby HUD on behalf of particular projects; if those projects get the subsidies, the owners can pay the consultants out of the subsidy. Thus these programs invite abuse. This happened in the Section 8 Mod Rehab program of the late 1980's.

The insurance also makes it hard for HUD to enforce the contractual responsibilities of the owners, because they always have the option of defaulting and forcing HUD to take over the project. HUD's role as insurer conflicts with its role as provider of housing assistance for the poor. Ultimately, HUD's role as insurer makes it the slumlord of last resort for the worst projects. For these good reasons, there has been no project-based assistance program since Section 8 New Construction was repealed in 1983. But HUD is still providing subsidies to 1.6 million households living in privately owned projects that were built before then.

(3) Public housing has a mixed record. Most PHA's appear to do a reasonably good job of providing decent housing for their tenants, and most projects are decently maintained. But many of the largest PHA's don't do a good job, and in many cities there are projects which are locally notorious as terrible places to live. Public housing is twice as expensive, per family per year, as a voucher or certificate, and in too many cases it provides much worse housing. Construction costs are now about $85,000 per unit, and operating subsidies and modernization have grown greatly over the years. For 1995 Congress appropriated $2.9 billion in operating subsidies, $3.6 billion in modernization, and $0.5 billion for "severely distressed" public housing, which is another form of modernization—a total of $7 billion. The House Appropriations Subcommittee has voted to rescind $2 billion of that amount, but even at the lower level, the growth rate has been rapid. In 1980, operating subsidies were $0.9 billion—they were being blamed on the energy crisis—and $0.5 billion worth of modernization was financed. The 1995 appropriations level is double the 1980 level, after allowing for inflation. Modernization especially sometimes seems to be a bottomless pit. Every few years there is a new study of modernization needs, and

Congress raises the annual appropriation in response; then a few years later there is another study, and it turns out that total modernization needs are higher than they were in the previous study, even after spending several billion dollars.

Management Deficiencies

HUD doesn't manage these complicated programs very well. The most serious administrative problem is that HUD does not have an adequate accounting and budgeting system for Section 8 projects. FHA does not know how much it should pay in rent subsidies to project owners. This problem was identified as HUD's "number one material weakness" in the last Administration, and a major effort was initiated to create an adequate system. Of necessity, development of the system carried forward into the present Administration. At a hearing before the House Oversight Subcommittee 2 weeks ago, the HUD IG said that "progress is slow."

The entire program area of FHA multifamily insurance has severe management problems, especially for programs combining project-based assistance and FHA insurance, and the IG has said that progress in other major management systems is still slower. In a hearing before the same Subcommittee last year, senior HUD officials acknowledged that they did not have adequate information about the physical condition of Section 8 projects, and could not say which ones needed major repairs. I believe that the Subcommittee on HUD Oversight and Structure can perform a major service by monitoring the development of these management and information systems closely, and urging HUD to greater efforts.

The Reinvention Blueprint

The best way to assess the Reinvention Blueprint or any other reform proposal is with regard to whether it builds on HUD's demonstrated areas of effectiveness and discontinues the programs where HUD has failed in the past. By this criterion, the Blueprint deserves one cheer.

SUBSIDIZED HOUSING

The most positive proposal in the Blueprint is a fundamental change in the structure of housing assistance for low-income families. Here the Blueprint shows an awareness of past problems and offers bold solutions. There would be a dramatic shift from project-based assistance to tenant-based assistance. The new system would rely on the free choices of low-income families in the private housing market. Operating subsidies and modernization funding would no longer be provided to public housing authorities, but instead the money would be given directly to the residents of these projects in the form of vouchers. The Blueprint would force PHA's to compete with private landlords for tenants. It would take away their guaranteed, captive, tenants, and subject them to the discipline of the housing market. The same policy would apply to the private projects—Section 8 New Construction and its predecessors—as their current contracts with HUD expire. And all future incremental assistance would take the form of vouchers or certificates.

These proposals make sense in budget terms as well as policy terms, and the Administration deserves credit for offering them. The cost of the voucher, per family per year, is about the same as last year's appropriation for operating subsidies and modernization in public housing. If each family living in public housing received the money HUD is now spending on operating subsidies and modernization, and continued to spend 30 percent of its own income on rent, it could afford anything renting at or below the FMR on the private market. This may not be true if the cuts proposed by the Appropriations Committee in the House are enacted, but there are several ways to cover any difference in cost.

There are some problems. The Blueprint does not allow for public housing residents to manage or own their projects. Many residents and resident organizations want to build viable communities of decent housing where they now live, and some have already done it. If residents want to own or manage their projects, they should be encouraged to do so and the Blueprint should be modified to offer that opportunity. If they do not, then they should be given the opportunity to live in decent housing of their own choosing, with a voucher.

Unfortunately, these desirable changes are not scheduled to happen for 3 years during the next Administration and the next Congress. The Congress may want to expedite that schedule; it can be done sooner. Meanwhile, public housing project development could be zeroed out in this year's budget. There is no reason to build more projects now, if the policy decision is to stop subsidizing them as projects three years from now.

THE INSURED ASSISTED INVENTORY

The Blueprint proposes to apply the same approach to privately owned projects, though on a slower timetable and with transition practices that are likely to be

counterproductive and costly. Costs in these projects are often higher than the cost of a voucher or certificate, and tenants have incomes about 15 percent higher on average than public housing tenants. Thus it is certainly likely that these projects can be converted to vouchers at savings to the taxpayer. The Blueprint proposal will work for their residents as well as for the residents of public housing.

As part of this process, the HUD budget proposes "dramatic changes" in the preservation program created by the Low-Income Housing Preservation and Resident Homeownership Act (LIHPRHA) of 1990. Commitments for continued subsidies to privately-owned projects would be scaled back to FMR levels, whereas LIHPRHA allows rents up to 120 percent of the FMR. Cutting back on subsidies that are out of line with market rents is highly desirable and can save the taxpayers substantial sums for many years.

But at the same time the administration is asking for authority to spend a great deal of the taxpayers' money in a misguided effort to avoid insurance claims. The Blueprint proposes to "mark to market" the insured assisted housing inventory, project by project. This would involve paying off part of the principal on the loans now, based on some estimate of what the projects are really worth. HUD wants to spend $643 million for this purpose in FY 1996. Marking to market will be immensely staff-intensive and immensely difficult to do well, for the same reasons that it's staff-intensive and difficult to underwrite multifamily mortgages in the first place. Moreover, these are exactly the programs where FHA's information systems are most deficient. HUD does not know enough to make sound decisions about the value of the projects.

The way to find out what the projects are really worth is to stop subsidizing them. Financial incentives to preserve private projects should be discontinued, instead of being extended to additional projects during a 3-year transition period. If the projects are going to have to compete with other privately-owned housing for tenants, that competition should start as soon as possible. This will be a gradual process as contracts and commitments expire or come up for renewal; most projects now have ongoing commitments from HUD.

I recognize that some privately owned projects may go into default without the project-based commitment. Where the projects carry FHA insurance, that will cost the Government money. It will still be cheaper to let that happen than to go on providing project-based subsidies, one on top of the other, in an effort to stave off default and avoid paying insurance claims.

Marking to market should be rejected. It is simply the latest example of the problems that arise when FHA multifamily insurance is combined with project-based assistance, and it is likely to have the same result. If HUD is allowed to start paying lenders off on the basis of its estimate of market value, the Oversight Subcommittee will have a fertile field for investigations in a few years.

FHA

With respect to FHA, the Blueprint is just backward. One might start to reinvent HUD by terminating the scandal-ridden and problem-plagued multifamily insurance programs, while leaving home mortgage insurance in place. The Blueprint does the opposite. FHA multifamily insurance would continue unabated and unreformed. So would the production of privately owned low-income housing projects, and perhaps public housing, through the HOME block grant, renamed the "Affordable Housing Fund." The Affordable Housing Fund is intended to be a production vehicle for lower-income housing. Cities and States will get money to build the same kinds of projects which have proven to be expensive and too often unsuccessful ways of providing housing assistance for the poor. There is no reason to believe that they will be able to build new projects that work any better than the ones now in operation. Moreover, since there are to be no more project-based subsidies, it's not clear how low-income tenants will be able to afford apartments in these new projects. Worst of all, the Blueprint envisions combining Affordable Housing Fund money with FHA insurance on the projects that cities or States finance with that money. After all the experience with these programs, why create a new one now?

While FHA would continue its complicated and expensive multifamily insurance programs, it would get out of the business of insuring home mortgages, which it does know how to do. The long-established Section 203 program would gradually be replaced by joint insurance schemes with private firms and State housing agencies. This is a fine way to lose money, as FHA has demonstrated in the past. In the 1980's it created a similar program for mortgages on rental properties. HUD shared insurance premiums and risks with private lenders, letting the lenders do the underwriting. When defaults occurred, it turned out that the lenders had no capital to meet their share of the losses, and HUD wound up taking the full loss. This has

been one of its costliest failures ever, and HUD is projecting a loss of 50 cents on the dollar for the coinsured loans still outstanding.

State housing agencies have more capital than the private lenders did, but splitting the risk is still an issue. The State agencies have always wanted the Federal Government to take the risk in any partnership with HUD. When HUD made a similar proposal in last year's housing bill, the House of Representatives wanted to limit FHA's risk exposure on each mortgage to 35 percent of the original amount borrowed, which is close to FHA's average loss on a defaulted mortgage, but the State agencies said the 35 percent limitation would "destroy the program." Fortunately, Congress didn't pass either version of it.

Whatever the legislated degree of risk sharing, even large units of Government can go bankrupt, as Orange County is now demonstrating, and nobody's pockets are as deep as the Federal Government's. The likely outcome of joint insurance schemes is that HUD would continue to bear all the cost of defaults, but with less premium income. If the market perceives that coinsurance dilutes the full Federal guarantee on the mortgage, homebuyers will face higher mortgage rates as well.

FHA insurance could be better targeted to lower-income families, say those in the lower half of the income distribution; as things now stand, families with incomes of $80,000 a year are eligible for Government-supported mortgage insurance in some parts of the country. That is a long way from the original clientele of young moderate-income families buying their first home. But for those young moderate-income families, FHA insurance serves a market that private insurers have so far not reached, and FHA serves it without losing money. FHA should not be protected from the private mortgage insurance industry; it is not protected now. But FHA's historic mission should not be compromised either.

Privatizing or Reorganizing FHA

These points are relevant for the issue of privatization, which the Subcommittees have listed as an issue for these hearings. Privatization is an important issue mainly for FHA. because it provides services which are also provided in the private sector. In fact, its original rationale was as a demonstration to the private sector of the viability of long-term self-amortizing mortgages with low downpayments, and of mortgage insurance.

In any privatization plan for FHA, the basic question is who has the right to commit the full faith and credit of the Federal Government. I believe it should remain with the Federal Government, and not be given to private entities or other levels of Government which will not have to bear the costs if they make mistakes. There is in addition the GNMA guarantee of timely payment of principal and interest on mortgage-backed securities, also a commitment of the Federal Government's credit which should remain exclusively a Federal Government responsibility.

Without the Government guarantee, FHA cannot insure mortgages for the full range of families that it is now serving. It would be no different from any other mortgage insurer. Private mortgage insurers are free to compete with FHA now, but they haven't been able to take all its business. As a private insurer, FHA wouldn't be able to insure some part of its present portfolio, any more than the private mortgage insurers can. Some families would have to postpone buying a home until they could make a larger down payment; a few might never be able to buy a home.

Alternatively, FHA could be turned into a quasi-governmental entity or a USE, along the lines of Fannie Mae and Freddie Mac. These firms do not have the full faith and credit of the Government behind them, but they have Federal charters and various privileges such as the ability to borrow from the U.S. Treasury in an emergency and exemption from State and local income taxes, and the financial markets certainly expect that the Government will not let them fail. The privileges enable them to obtain funds at lower rates in the capital markets than banks or savings and loans, so they can in turn buy mortgages and issue mortgage-backed securities at lower rates. They are highly profitable. A "Government sponsored" FHA could have some comparable privileges which would give it an advantage over private mortgage insurers, and perhaps comparable profitability as a result. It would become difficult for private mortgage insurers to compete for business that they now serve quite adequately. Also, as a profit-making institution, FHA's motivation would be different than it is now. It would probably concentrate on mortgages with less risk than its current portfolio, because they would be more profitable.

If FHA is privatized, or if it becomes a USE without the full faith and credit of the Federal Government behind it, it will not be able to continue its multifamily programs in their present form. At present FHA multifamily insurance is really a disguised subsidy, which a private firm could not afford. Congress would have to appropriate explicit subsidies.

The Reinvention Blueprint proposes a third approach: turning FHA into a "Government-owned, streamlined, market-driven" corporation within HUD. The rationale for this change is improved efficiency. But FHA's efficiency does not depend on its legal status. The Postal Service is a Government-owned corporation. It is neither streamlined nor market-driven. For that matter, FHA was an independent Government agency for three decades. There were scandals in the multifamily mortgage insurance programs of FHA before it was part of HUD, and there's no magic in a Government-owned corporation to prevent scandals in the future.

What Should Be Done?

HUD now has effective programs to serve each of the basic purposes of housing and urban policy, but it also has ineffective programs to serve some of them, and programs whose relationship to public policy objectives is marginal at best. Genuine reform of HUD and housing policy can and should be built on the effective programs. HUD could continue to insure single-family home mortgages through FHA (and securitize them through GNMA) to promote home ownership; give vouchers to low-income families so they can afford decent housing that they want to live in; and give State and local government whatever funds it can afford for community development in one block grant, with few or no strings, to help them create suitable living environments. These things are being done reasonably well at HUD now, and each of them serves a public policy purpose.

At the same time, HUD should stop doing the things it has not done well for several decades. It should stop insuring multifamily mortgages, stop subsidizing the construction and the operation of low-income housing projects (either directly or through a block grant), and above all stay out of the tempting quagmire of combining multifamily insurance with project-based subsidies.

Terminating multifamily mortgage insurance may sound drastic, but in fact FHA does not serve a particularly large share of the multifamily market. In 1993, the last year for which the full data are available, FHA insured about 5 percent of all multifamily mortgage originations—$1.6 billion out of $30 billion; and about 7 percent of all new apartments—9,000 out of 127,000. It is a small program for all the headaches it causes at HUD.

If Congress directs HUD to concentrate on what it can do well, you will achieve a fundamental reform of housing policy, and really "reinvent" HUD in the process. By comparison, the Reinvention Blueprint is only a partial reform. It would terminate the subsidies for the operation of subsidized projects that have already been built, but this would be offset by reviving FHA insurance for new subsidized projects, and all of HUD's other problem areas would be untouched. At the same time, it would "fix" FHA home mortgage insurance, which isn't broken, by creating new and complicated programs that are likely to be less effective and more costly than the current Section 203 program.

It's certainly possible to make these substantive changes in housing policy and abolish HUD in the process. FHA home insurance, the voucher program, and the Community Development Block Grant could all be administered by other agencies. But since they are being done reasonably well at HUD now, there's no particular advantage to dismantling the Department, and there is a substantial cost—not in dollars as much as in the time and effort that would be devoted to reorganizing the program offices in new agencies. The fundamental question is "What should the Government do in housing and community development?" Once that is resolved, the question of what agencies should perform those functions can be considered systematically.

Thanks to the 1994 election and the Administration's reaction to it, there is a real chance to reform HUD. It will take more real changes than the Administration has proposed, and it can't be accomplished merely by abolishing HUD unless real changes are made as well. But if those real changes are made, then homebuyers, the poor, and other people who benefit from HUD programs will have reason to be grateful, and so will the taxpayers.

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WHY KEEPING HUD IS A GOOD IDEA

Introduction

In Washington today, major political efforts are underway to eliminate, or at least drastically shrink, the U.S. Department of Housing and Urban Development (HUD). Since HUD spends around $26 billion per year on a great many different housing and other programs, and since most of that money flows into real estate markets around the Nation, HUD's elimination would have notable effects upon money flows into U.S. real estate markets. For this and other even more cogent reasons, I believe it is in the public interest to maintain a separate Federal department concerned with housing and urban development—even if the way it performs its functions is radically changed. This article presents my arguments supporting that conclusion.

HUD's Housing Missions

HUD was created in the late 1960's during the Johnson Administration through the consolidation of several previously separate agencies dealing with housing, housing finance, and urban mass transit. HUD has since evolved through the addition of many more housing programs to its purview, and the removal of urban mass transit to the Department of Transportation. A recent HUD document officially defines HUD's basic missions as follows: (1) assisting homeless persons and families, (2) reducing the number of distressed public housing units, (3) developing affordable housing and making home ownership a reality for more Americans, (4) reducing racial barriers in housing markets, (5) empowering communities—especially poor ones, and (6) creating an environment (within HUD itself) that supports teamwork and organizational excellence. The first four of these missions all deal directly with housing, and the last two do so indirectly. It is therefore clear from these missions that *one of HUD's central purposes is improving the housing situation of the American people, especially poor people who cannot afford "decent" quality housing without aid from others.*

Why HUD Is Needed to Perform Those Housing Missions

Why does the Nation need a separate Federal department to pursue the housing missions described above? For one thing, living in adequate housing is a central element in the wellbeing of every person and household. Yet housing is the single costliest element in people's basic living standard. Consequently, millions of households with low incomes cannot afford to occupy "decent quality" housing if they must rely solely upon their own resources. Therefore, insofar as the Federal Government is concerned with its citizens' well-being, it must be concerned with improving the quality and quantity of their housing.

But no other agency within the Federal Government focuses on housing as part of its central mission. Ally other Federal agencies are concerned with housing only peripherally, if at all. So no others are likely to pay enough attention to housing to improve the chance that most citizens will be well-housed. Only a separate department with that mission as one of its central purposes will have such a focus.

Why not leave this element to State and local governments? A key reason is that providing housing aid to poorly housed citizens amounts to redistributing resources from others to those citizens. But all resource redistribution schemes are more effectively *financed* (though not necessarily best *administered*) at the national level. Local governments cannot tax their better-off citizens highly in order to aid their poorer citizens without causing many of the former to move away to nearby communities that have no such redistributive schemes. Even State governments suffer from that competitive disadvantage. This is shown by the tax-induced flight of many firms from high-tax New York to neighboring Connecticut and New Jersey. Only the Federal Government can impose higher taxes on its wealthier citizens to aid its poor ones without causing many of the former to move elsewhere. (Even that is hard to do politically in times of relatively slow household income growth, such as the past 20 years, because taxpayers then resent such redistribution.)

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[1]The views in this article are solely those of the author, and not necessarily those of The Brookings Institution, its Trustees, or its other staff members.

Furthermore, the cost of a household's financing a home purchase is heavily influenced by mortgage interest rates and mortgage fund availability. Those conditions are determined by *national* financial conditions and markets, not *State* or *local* ones. Therefore, it is necessary to have an agency with nationwide scope and authority to deal with housing financial conditions and availability, rather than having multitudes of parochial State or local agencies try to do so.

Similarly, the racial and ethnic discrimination and segregation that permeate American housing markets cannot be dealt with effectively by purely State or local agencies. Those narrower-jurisdiction agencies need the legal empowerment of national anti-discrimination and anti-segregation laws and policies to support local enforcement efforts. For the same reason that the civil rights movement ultimately required Federal action to overcome powerful State and local resistance, policies attacking racial barriers in housing markets also need a strong national agency dedicated to that mission. It must be equipped with powers that transcend locally dominant prejudices.

For all these *housing-related reasons*, the Nation needs a separate Federal agency dedicated to the housing missions described earlier above.

HUD's Urban Development Missions

In addition, I believe HUD has another central set of missions related more to *urban development patterns* than to housing in itself. Almost 80 percent of Americans live in metropolitan areas, each containing one or two central cities and their surrounding suburbs and "exurbs." The basic economic, social, and other functions of American society are therefore mainly carried out within these over 330 metropolitan areas. If American society is to function well enough to provide its citizens with "decent" living standards and a satisfactory quality of life, its activities must be located in space in ways that promote the mutual efficiency and effectiveness of those activities. Therefore, *the spatial efficiency of how activities function within metropolitan areas is of vital importance to our entire society.* If those activities are located in ways that greatly reduce economic efficiency, increase social conflict, or isolate whole groups of citizens from receiving proper schooling or job opportunities, the results can be very harmful to our whole society.

Yet no existing State or local governments, and almost no regional ones, have any direct responsibility to help insure the appropriate spatial efficiency of activities within our metropolitan areas. True, many metropolitan areas lie entirely within a single State. Therefore, in theory, that State's government could take upon itself some responsibility for improving the spatial efficiency of activities within its metropolitan areas. But few States have assumed that responsibility. And many of our largest and most important metropolitan areas lie within two or more States. Examples include New York, Boston, Washington, Chicago, Philadelphia, St. Louis, Memphis, Cincinnati, Charlotte, Louisville, Kansas City, and Portland (Oregon). These metropolitan areas contain 22.4 percent of the Nation's total population. No one State can have jurisdiction over their overall efficiency.

Trends Undermining the Spatial Efficiency of American Society

Why do we need to worry about the spatial efficiency of our metropolitan areas? Because current trends are seriously undermining that efficiency in many of our largest metropolitan areas in ways that local governments cannot halt. The fragmentalized government structure in nearly all U.S. metropolitan areas makes it impossible to develop coherent, consistent, and effective policies toward several key growth-elated problems. These include air pollution and other environmental degradation, traffic congestion, provision of sufficient new infrastructures to accommodate growth, selection of sites for regionally necessary facilities like airports that have negative impacts upon their immediate surroundings, and the absorption of excessive open space.

All of these problems are essentially regional or metropolitan-area-wide in nature. But they are all related to the patterns of land uses emerging from on-going urban development controlled by fragmentalized local governments. That is why HUD's spatial efficiency mission—which focuses on land use patterns—is relevant to problems like air pollution that technically fall under the jurisdiction of other agencies, such as the Environmental Protection Administration. At present, power over land uses and other regulations that would need to be coordinated to cope with such regional problems is divided among hundreds of local governments. Moreover, each such government is competing with all the others to capture activities that generate net local tax revenues, and to reject activities that generate net local fiscal losses. This ferocious fiscal competition makes development of a single coordinated land-use policy among local governments almost impossible.

The result is an immense spreading of people and activities across the landscape that increases the need—and cost—of travel within each metropolitan area. In the 20 years from 1970 to 1990, the Chicago metropolitan area gained only 4 percent in population, but increased over 40 percent in urbanized area. Similar "de-densification" occurred in dozens of other major metropolitan areas. It is no accident that total vehicle miles traveled in the U.S. rose 37 percent from 1983 to 1990, compared to a rise of only 4 percent in total population. More and more time and resources are now being consumed by travel, often waiting in creeping lines of congested traffic. This is a sign of decreased overall spatial efficiency.

Much more important in the long run is the deteriorating fiscal and social condition of many major central cities and older close-in suburbs. As rapid growth on the fringes of each metropolitan area draws the most prosperous and viable households and firms out of central cities and older suburbs, those communities are left with declining per-capita tax bases and increasing concentrations of poor households with high public service needs. In 1990, the Nation's central cities contained only 31 percent of the entire U.S. population, but 42 percent of all poor persons. Within all central cities combined, about 19 percent of all residents were poor, compared to about 8 percent in suburbs as a whole, and 14 percent in the entire Nation. This concentration of poverty is greatly influenced by the exclusionary policies of many suburban local governments. They erect zoning, building-code, and other regulatory barriers to the creation of any added low-cost housing within their boundaries in order to keep "the wrong kind of people" out of their neighborhoods. That forces high fractions of all poor residents to live in central cities and older suburbs that cannot engage in such exclusionary behavior. This situation loads local governments in older central cities and suburbs with increasingly unbearable fiscal burdens and extensive areas of deteriorating or abandoned neighborhoods.

Furthermore, central cities and older suburbs contain a majority of members of two large minority-groups that will play ever-more-important roles in the Nation's future. These are African-Americans and Hispanics. Together, the 58.3 million persons in these two groups comprised 22.2 percent of the Nation's total population in 1995. *But they will make up 56.2 percent of the projected 58.3 million increase in population between 1995 and 2020.* So in 2020, just 25 years from today, these two groups will comprise 28.5 percent of our total population. At present, the average household incomes of these groups are between 30 percent and 40 percent below those of non-Hispanic whites, and the educational attainment of the former two groups is similarly below that of the last. Unless this condition is changed in the future, most of the Nation's future population growth will occur among its poorest and least skilled major minority groups. To improve their incomes and skills, American society needs to improve the quality of education and the job opportunities available in the central cities and older suburbs where most of these groups live. But that will be extremely difficult if continued future peripheral growth of our metropolitan areas keeps on draining economically strong households and businesses out of those central cities and older suburbs.

Our Failure to Recognize the Need to Improve Spatial Efficiency

Right now, no government or private groups anywhere within our society—except HUD—are officially entrusted with the mission of thinking about, or doing something about, these adverse trends. Even HUD has not focused much of its past attention on developing policy responses to such trends. Since the Clinton Administration took office, HUD Secretary Henry Cisneros has talked a lot about responding to these metropolitan-area trends. But in reality, HUD has not re-focused its missions to include strong emphasis on improving the spatial efficiency of metropolitan areas, as its above-quoted mission statements show.

Nevertheless, American society needs some highly visible, politically active public focal point for thinking about, and improving, the spatial efficiency of our metropolitan areas. An important aspect of such improvement would be creating incentives for the development of some type of regional-decisionmaking within each metropolitan area. That does *not* mean metropolitan government. Rather, it means at least some type of planning for functional activities (such as housing, health care, and transportation) that takes account of the needs of *each region considered as a whole,* not just each locality considered apart from all the others. An example is the metropolitan planning requirement concerning highways and mass transit adopted by Congress in the Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA, often referred to as "Iced Tea"). A similar regional planning requirement might eventually be connected to the housing and other programs under HUD's jurisdiction, as a means of improving the spatial efficiency of our metropolitan areas.

HUD is the logical body to take on the challenges associated with such improvement, because its official area of jurisdiction includes both housing and urban devel-

opment. HUD needs to provide leadership in focusing the Nation's attention on the need for region-wide approaches and policies aimed at coping with the region-wide problems described above. If HUD does not take on this mission in a powerful way, the adverse trends described above will further weaken many older central cities and suburbs and cause calamitous decay in large parts of our inner-city neighborhoods.

This conclusion does *not* imply that HUD alone can solve all the problems associated with declining cities and deteriorating inner-city neighborhoods. Even at best, it could not do so without help from many other parts of society, both public and private. But if HUD does not exist to at least focus public attention on these issues, few—if any—remedial policies will be directed at them.

Conclusion

American society needs to retain the U.S. Department of Housing and Urban Development as a separate Federal agency because it needs someone to perform two crucial missions now entrusted to HUD. One is up-grading the housing of the population; the other is improving the spatial efficiency of our metropolitan areas. Both these missions are vital to the future quality of life in our society. But no other agencies—public or private, Federal, State, or local—are likely to focus on those missions in the future.

This conclusion does not mean that HUD should remain in its present form, or do business "in the same old way." Many of the radical changes in HUD and its operations now being proposed by HUD's leaders themselves and by Congress are certainly worthy of serious consideration. But I believe completely eliminating this agency, or weakening its ability to pursue the two central purposes discussed above, would be a disservice to the Nation.

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WASHINGTON, DC

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Introduction

Carried into office by an electorate demanding fundamental change in failed social welfare programs, Members of the new Congress have targeted the costly and counterproductive housing programs of the U.S. Department of Housing and Urban Development (HUD) as a top reform priority. Sensing the electorate's demand for change and the commitment of the new Congress, HUD Secretary Henry Cisneros Jr. issued last December 19, 1994 his *Reinvention Blueprint,* which offered a stinging critique of HUD and a commitment to restructure it's programs in the direction first established by the Reagan Administration. But when President Clinton's FY 1996 budget proposal was released on February 6, 1995, it was apparent that the only thing that had changed was the rhetoric, and the failed programs of the past would continue to receive generous funding for the foreseeable future. The President's FY 1996 HUD budget should be rejected, and Congress should proceed with its own plans for the fundamental overhaul of America's housing policy. Such an overhaul should begin with the dissolution of HUD.

As this statement will argue, a strong case can be made for the dissolution of HUD for reasons far more important than any near term budgetary savings or deficit reduction targets. With the vast majority of its programs focused on low- to moderate-income households, HUD is an integral part of the Nation's failed welfare system. For this reason any changes made to HUD must be consistent with the welfare reform goals of ending long-term dependency and creating strong incentives for self-sufficiency.

Of the many possible directions that welfare reform could take, the one now favored by a significant number of House and Senate members is to shift the welfare responsibility and the necessary financial resources to the States in the form of block grants. The housing assistance responsibilities and resources that now belong to HUD and comprise about 80 percent of its budget, should be part of these block grants. Legislation introduced by Senator Lauch Faircloth (R–NC), and Representative James Talent (R–MO) would accomplish this objective. The other non-means tested programs operated by HUD should be terminated, transferred, or privatized, as discussed later in this statement.

Created in 1965 out of several existing Government entities involved in housing, mortgage finance, and urban issues, the creation of HUD was the Federal Govern-

ment's response to the emerging urban crisis that had manifested itself in a series of destructive and deadly inner-city riots. The concern then, as it is today, was the emergence of an impoverished urban underclass subject to low educational attainment, family dissolution, unemployment, high crime, poor health, and inadequate housing.

As the unfortunate record indicates, and despite the spending of more than $5 trillion in means-tested assistance by HUD and other Federal agencies since 1965, our urban problems are worse and the number of low-income, non-elderly households is not materially different today than it was back then, although the environments in which many live are far more dangerous and despairing.

HUD is just one of many weapons brought to the battle by the Federal Government, which in the years since has marshaled the resources and attention of most of its domestic departments in the fight against poverty and the ills of the declining cities. Along with HUD, the Departments of Agriculture, Health and Human Services, Labor, Education, and Justice provide food stamps, Medicaid, Aid to Families with Dependent Children, education and law enforcement grants, job training and a host of other programs. In FY 1993, the most recent year in which complete estimates have been made, such means-tested spending amounted to a staggering $324 billion dollars, of which a little under $30 billion was for housing aid, and urban and community development programs, mostly operated through HUD.[1]

Housing Reform as a Component of Welfare Reform

The welfare system we have created is costly and administratively intensive at all layers of Government. Rather than directly addressing the chief problem—inadequate incomes and their cause—with an administratively simple solution—cash grants along with strong incentives to become productively employed and to take full responsibility for one's life and family, we instead choose to focus mostly on symptoms—poor diet, poor health and poor housing—and have, in turn, created a costly administrative infrastructure, particularly with regard to housing assistance, that bureaucratically attempts to address each: Food stamps to improve your diet, Medicaid to improve your health, Job Training Partnerships to get you to work, and dozens of HUD programs to improve your housing.

Although the focus of this paper is on HUD and its housing programs, any fundamental reform of the housing assistance programs must be accomplished within the context of overall reform of the Federal welfare system, and that the key components of that reform must include strong incentives for self sufficiency, consumer choice, administrative efficiency and work requirements for able-bodied, non-elderly recipients.[2]

At present, with its emphasis on project-based assistance which collects the needy in Government-subsidized and Government-operated housing projects, the housing component of our welfare system largely fulfills a custodial function, often segregating the poor in out of the way places with high crime and few job opportunities. What is needed instead is a system that diminishes the number of poor, and HUD, whose programs are largely targeted to low-income households and communities, must be a part of this new system.

Although there is some overlap, HUD's programs operate in four main functional areas covering (1) Low-Income Housing Assistance, (2) Community Development Block Grants, (3) Mortgage Insurance (the FHA and GNMA) and (4) Fair Housing. The low-income housing assistance programs are HUD's largest functional area and absorb about 80 percent of HUD's budget through a variety of different programs. Most of the remaining twenty percent of HUD's budget is spent on the Community Development Block Grant program, which covers a variety of civic purposes, including housing. The FHA's single-family mortgage insurance functions have generally been self-financing over the long-term, while the budget for Fair Housing activities is just a small fraction of the first two.

In recognition that much of HUD's programs are already operated through State and local housing authorities under HUD's guidance and directives, this paper proposes to merge all **low-income housing assistance programs** into a single welfare block grant for the States, and that the States be encouraged to administer that portion of the grant they allocate to housing assistance in the form of housing vouchers and certificates that permit the eligible households to choose where they want to live, and that the States also be encouraged to allow the tenants and pro-

[1] *"The Scope of the Welfare State"* by Robert Rector, The Heritage Foundation, Testimony before the Committee on Government Affairs, U.S. Senate, January 25, 1995, pp. 2–3.

[2] *"Four Themes of Welfare Reform," by Robert Rector, The Heritage Foundation, testimony before the Committee on Economic and Educational Opportunities, U.S. House of Representatives, January 18, 1995.*

gram beneficiaries much more involvement and control of the management and ownership of the Government-owned projects they live in.

The **Community Development Block Grant** program, which has been spending between $4 billion and $5 billion per year on a variety of different purposes, including housing assistance, would be made redundant by the above proposed housing block grant and thus should be eliminated.

The single-family mortgage insurance programs of the **Federal Housing Administration (FHA),** would be reorganized into an independent government corporation while its portfolio was cleaned up in preparation for eventual privatization. Much of the FHA's recent financial difficulties have been largely due to costly defaults and foreclosures of FHA insured mortgages on the subsidized, multifamily housing projects.

Finally, HUD's **Office of Fair Housing,** whose chief purpose should be to prevent housing discrimination, would be transferred to the civil rights division of the Justice Department where the issue can be more effectively and efficiently pursued in the context of overall civil rights enforcement.

By establishing block grants and encouraging that the funds provided be utilized primarily for household-based assistance, rather than the project-based assistance that now dominates the HUD programs and are twice as costly per household served, the Government would be able to provide higher quality assistance to more people at less cost. At the same time, by linking the housing assistance to overall welfare reform, we can begin the process of moving people to self-sufficiency and ending the long-term dependency that has come to characterize many of these programs.

Reforming the Governments Involvement in Housing: Additional Details

Low-Income Housing Assistance. Since the early seventies much of the debate over housing policy has been between the advocates of project-based assistance versus those who favor household-based assistance. Arguing that an individual's apparent housing problems—defined as substandard housing, overcrowding, high rent payments to income, etc.—are in fact income problems, advocates of household-based assistance propose to improve housing conditions by providing eligible households with the financial wherewithal to acquire better housing. While a cash payment would be the most efficient way of rectifying the problem, in practice the assisted household is given a cash equivalent in the form of a voucher or certificate that can be used to pay the rent or some portion thereof in suitable apartments provided by private sector landlords or other entities.

As such, a housing voucher program largely conforms to the process and purpose of most other Government assistance programs such as food stamps, student loans, Medicare and Medicaid, and unemployment compensation. In each of these programs, Government provides the eligible individual with the means to acquire the product or service, but the actual product or service is generally provided by the private Sector, nonprofit institutions or State and local governments.

The alternative to household-based assistance is project-based assistance where the Government subsidizes through a variety of mechanisms the construction, renovation, acquisition and/or operation of multifamily housing projects where some or all of the units are reserved for occupancy by low-income households. At present, approximately 70 percent of those who are assisted through HUD program's are in the project-based programs, while the other 30 percent are in household-based programs such as vouchers and certificates.[3]

The advantages of a household-based program over those that are project-based are chiefly of two types. First, household-based assistance is about half the cost of project-based financing.[4] The table below, which was compiled by the Office of Management and Budget for President Reagan's Commission on Privatization, provides the 20-year costs per household assisted for several of the major housing programs. The first two are household-based, while the next four are project-based, and include an Agriculture Department program for qualified residents of rural areas.

[3] "*The Challenges Facing Federal Rental Assistance Programs*" A CBO Study, The Congressional Budget Office, December 1994, p. xiii.

[4] "*Privatization: Toward More Effective Government,*" Report of the President's Commission on Privatization, March 1988, p. 11.

Program	20-Year Cost
Voucher	$27,892
Section 8 Certificate	$27,955
Farmer's Home Section 515	$35,210
Rental Housing Development Grant	$53,500
Section 8/292 Housing	$53,575
Public Housing	$69,863

Source: Report of the President's Commission on Privatization, Table 3, p. 11.

Inasmuch as HUD housing assistance programs are not entitlements, but operate on a first-come first-served basis which leaves many eligible low-income households unassisted, any reform that improves program efficiency also increases the number of beneficiaries for the same total costs, or less.[5]

The second major benefit is that the vouchers are portable and allow the recipient a measure of choice in finding suitable housing to rent. In this way, assisted households can integrate themselves in the community at large according to their own interests and needs, permitting, for example, a family with young children to make neighborhood choices with regard to schools, or an elderly individual choices with regard to family and friends.[6] In contrast, project-based assistance concentrates the assisted, and thus largely the poor, in segregated settings that often are unsafe and distant from job opportunities and good schools. According to a recent CBO study:

> ". . . the evidence presented in this analysis suggests that with the exception of the elderly, recipients of household-based aid are less likely than recipients of project-based aid to be dissatisfied with their housing units or the condition of their neighborhoods. That pattern is apparent even though the incidence of substandard or crowded units is roughly the same for both types of aid among households of the same type."[7]

Efforts to integrate project-based assistance into better parts of the community usually meet with intense community resistance out of fear that such a large number of poor concentrated in one or two buildings would destabilize the neighborhood.

These benefits have not been lost on officials at HUD, and previous Secretaries from both parties have attempted to shift resources from the project-based programs to those that are household-based for all of the reasons cited above. Unfortunately, past Congresses, often influenced by special interests in the housing industry and within the local public housing authorities, have been successful in directing the bulk of HUD spending toward costly and inefficient subsidized housing projects.[8]

Vouchers and Tenant Empowerment. Besides the advantage of cost, another important benefit of vouchers is the locational and qualitative choices that this gives eligible households, and the extent to which this process of making *choices* can be creatively used to help resolve the question of what to do about the 70 percent of assisted households that live in public housing or subsidized projects. In his *Reinvention Blueprint* Secretary Cisneros' proposes to shift away from the past practice of providing financial support directly to the owners and managers of public housing, and instead, provide it indirectly by giving portable vouchers to the tenants

[5] CBO study, p. xiii.

[6] While many see this outcome as an advantage of vouchers, this view is not universal among housing analysts. In the January/February 1995 issue of The New Democrat, Howard Husock of the John F. Kennedy School of Government at Harvard University writes that "Rent subsidies, which now go to more than one million households, aim at dispersing poor families rather than concentrating them. In practice, this has often meant injecting the problems of public housing into previously stable neighborhoods."

[7] CBO study, p. xix.

[8] Last year's Senate appropriation bill is illustrative of the extent to which the bulk of HUD's resources were directed by Congress to programs already judged as costly failures. The bill allocates $598 million to public housing development, $300 million to Indian housing, $3.8 billion to the renovation and modernization of public housing, $1.7 billion to project-based housing for the elderly and disabled, $250 million for preservation, $555 million in property disposition costs, $500 million in the project-based Neighborhood LIFT program, $3.7 billion in expiring Section 8 contracts (a majority of which are project-based), $2.9 billion in public housing operating subsidies, $500 million for severely distressed public housing, $1.5 billion for the HOME Investment Partnerships Program, also largely a project-based program, and $350 million in grants to eliminate drugs and crime from public housing. The later item is indicative of just how deeply HUD has gotten sucked into sustaining costly failures, spending for basic law enforcement purposes absorbs funds that would otherwise have provided housing assistance to another 80,000 needy households. What is leftover for household-based assistance is a fraction of this, largely comprised of the $2.1 billion for incremental housing assistance, and some minor portion of the $3.7 billion for expiring Section 8 contracts.

of public housing projects. In this way, tenants could move elsewhere if they are not satisfied with the way their project is managed, and public housing authorities would be forced to improve services to maintain funding through tenant rent collections rather than direct Federal subsidies.

Congress should take this proposal another step further by giving the tenants several more choices—the opportunities to use their vouchers to manage and/or own the project where they live in a process that has already proven to be successful in dozens of public housing projects throughout the country. Initiated during the Reagan Administration and pursued more aggressively during the Bush Administration by Housing Secretary Jack Kemp, tenant management and ownership of public housing projects has proven to be a major success and has led to the transformation of decaying, drug and crime infested projects into safe and livable communities.

Experience has shown that with management or ownership in the hands of the residents, and with tenants empowered to shape the outcome of events and bear the consequences of their mistakes or inaction, the quality of life and service in these projects improves dramatically, regardless of how bad the situation was at the start. Kenilworth-Parkside in Washington, DC, Bromley-Heath in Boston, individual buildings in Chicago's Cabrini-Green project, Louisville's College Court and the Cochran Gardens in St. Louis represent just a few of the tenant management successes in otherwise hostile environments.[9]

Despite this record of success and the opportunity to turn adversaries into partners, this Administration has relegated the tenant ownership and management program to a back burner and, with the encouragement of past Congresses, has substantially reduced the funding available for tenant ownership planning and implementation grants. During the last budget cycle, HUD received more than a hundred bona fide requests from public housing tenant associations in partnership with their local PHA for grants to implement home ownership plans, but only eleven could be awarded because of funding limits.

This neglect could be rectified under the welfare block grant proposal by encouraging governors and mayors to utilize some portion of the funds to pursue tenant-based solutions to persistent public housing problems. Inasmuch as the public housing projects are owned by State and local governments, block grants get the Federal bureaucrats out of the loop and allow for more effective, local-based solutions.

Community Development Block Grants. After the assisted housing programs discussed above, the next largest component of the HUD budget is the Community Development Block Grant (CDBG) program. These grants, which are received and Spent on the basis of local priorities, include the acquisition and disposition of real property, construction of public facilities, rehabilitation of housing and the provision of a number of permitted public services. To be eligible, at least 70 percent of the funds received by a grantee must benefit individuals of low- and moderate-incomes.

As in the case of the programs discussed above, CDBG grants are largely project-oriented and subject to all of the criticism discussed earlier, except that there is much more of a pork barrel flavor to this program than to the project-based housing programs, and many CDBG projects appear to be of questionable value. One recent report noted that included on a list of "critical and ready to go" projects compiled by big city mayors was $1.2 million for an "arts center" in San Francisco, $250,000 for a central compost facility in Kalamazoo, MI, $400,000 for carousel renovations in Providence, RI, $360,000 for a swimming pool in Columbia, SC, and $200,000 for a sports complex and historic mill in Central Falls, RI.[10]

But such waste is only part of the problem. Implicit in the provision of such grants, whether for frivolous purposes or not, is the presumption that communities can spend their way to prosperity and that the only impediment to economic development is the absence of a few more infrastructure projects that would attract jobs, technology, and investment capital. We have long since stopped believing this about foreign aid and should now extend the same skepticism to our domestic bricks and mortar development initiatives such as the Community Development Block Grants, the Economic Development Administration, the Appalachian Regional Commission, and the Pennsylvania Avenue Development Corporation, to name several of the largest.

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[9] For more details on tenant ownership and management of public housing, see "Jack Kemp's "Perestroika": A Choice Plan for Public Housing Tenants," by Carl F. Horowitz, The Heritage Foundation, Backgrounder #888, March 26, 1992, and "The Misplaced Assault on Resident Ownership of Public Housing," by Carl F. Horowitz, The Heritage Foundation, Backgrounder #916, October 2, 1992.

[10] "Liberating the Poor From HUD's House of Privilege," by Tom Humbert, The Alexis de Tocqueville Institution, July 26, 1993.

In the last few years a new class of local leaders has emerged who recognize that the cities have often been their own worst enemies and that the high-cost of low-quality municipal services has been the one of the main reasons why businesses and middle-class families have fled the cities and continue to do so in response to gross mismanagement. But new mayors in Philadelphia, Milwaukee, Los Angeles, Indianapolis, Cleveland, New York, and Charlotte, and Governors in New Jersey, Massachusetts, and Wisconsin, to name just a few, have come to recognize that the key to their own development is not millions of dollars of federally funded projects but tax relief for their productive citizens, secure property rights through less crime, more efficient Government that delivers quality services at the lowest price, welfare reform that ends long-term dependency, and a functioning school system.

These initiatives can only be implemented by local leaders, not by Washington. Indeed, to the extent that Washington's money can temporarily patch over problems or pretend to address needs, there is less incentive for local leaders to make the tough decisions needed to solve their problems. For these reasons, the CDBG program should be terminated in favor of local-based reforms that create an environment that encourages business and productive citizens to remain in, or return to the cities.

Federal Housing Administration. The Federal Housing Administration (FHA) was created in the 1930's to promote the then innovative long-term, fixed-rate, level payment, fully amortized mortgage, and to fill the mortgage insurance gap created by the depression-induced collapse of the private mortgage insurance industry. Today, FHA competes with many private, taxpaying mortgage insurers for the profitable business of insuring mortgages on single-family residences. While for most of its history the single-family portion of FHA has been financially healthy, significant losses were incurred in the 1980's as the real estate market turned down in some regions of the country. Since then, as a result of an improved real estate market and program reforms, financial solvency has returned to the program and its net worth is estimated at over $4 billion.[11]

In addition to its single-family business, FHA also insures multifamily residential mortgages used to finance low- to moderate-income subsidized housing projects that were constructed under various HUD programs in cooperation with nonprofit and for profit developers. In recent years, many of the poorly conceived and mismanaged multifamily housing projects have gone into foreclosure, leaving FHA and HUD with multibillion dollar losses.

This report proposes that the financially sound portion (single family) of FHA be privatized, and that the remaining risky, unsound insured multifamily mortgages be pulled from FHA and placed in a separate liquidating facility and the insurance obligation on these multifamily loans be transferred directly to the Federal Government. Otherwise, the ongoing risk of these multifamily mortgages might eliminate any private sector interest in acquiring FHA or diminish its price. It should be noted that there is precedent within HUD for such asset and obligation transfers to enhance the attractiveness of enterprises slated for privatization. In the late 1960's when the Federal National Mortgage Association (FNMA, and then a part of HUD) was scheduled for privatization, its risky, subsidized multifamily mortgages were transferred to a newly created entity within HUD, called the Government National Mortgage Association (GNMA), for an orderly liquidation.

Opponents of the above proposal would argue that the FHA is largely responsible for insuring the mortgages of creditworthy but moderate-income households who might otherwise not be of interest to private mortgage insurers. They further argue that promoting home ownership is still a national goal, and to the extent that FNA can help accomplish this at no cost to the taxpayer and without offering unfair competition to private insurers, then FHA should remain within the Government in the belief that if privatized, it would turn away the otherwise creditworthy households of modest means. To the extent that this claim has validity, then a reconstituted FHA could be chartered as an independent government corporation (similar to FNMA) with no claim on the U.S. Treasury, required to be self-funded, and limited to those households and houses that might otherwise be neglected by the private Sector.[12]

Whether private or an independent government corporation, it is essential that a reformed FHA be free of day-to-day Government meddling. Otherwise, FHA will

[11] *"Mortgage Financing: Financial Health of FHA's Home Mortgage Insurance Program has Improved,"* Report to the Chairman, Subcommittee on Housing and Community Development, Committee on Banking Finance, and Urban Affairs, House of Representatives, U.S. General Accounting Office, October 1994. p. 4.

[12] See *Privatization: Toward More Effective Government,* pp. 30–32 for a more detailed discussion and proposal for an FHA better targeted toward buyers of moderate incomes.

continue to be exposed to the claims of special interests who, acting through previous Congresses and Administrations, induced FHA to insure risky high loan-to-value mortgages, vacation homes, private investment properties and risky, subsidized multifamily projects.

Office of Fair Housing. HUD's Fair Housing program is tasked with the goal of enforcing the Nation's fair housing laws and objectives, particularly as they relate to the ongoing problem of racial discrimination. Notwithstanding the considerable progress that has been made in this effort since the enactment of civil rights legislation in the 1960's, the problem persists and Government has an obligation to enforce the law and encourage landlords, builders, and real estate agents to obey it.

Unfortunately, in attempting to meet this goal, HUD bureaucrats have trivialized the objective, and in their pursuit of subliminal violations, have subjected the goal of nondiscrimination to ridicule.

How silly is HUD's effort? In response to HUD's directives, the Virginia Association of Realtors, for example, recently urged its member agents to use "caution" in the use of such words and phrases as *desirable neighborhood, handyman's' dream, near country club* (although "near golf course" is deemed acceptable), *prestigious, quality neighborhood, secure,* and *within walking distance.* Listed as "unacceptable" are such expressions as *able-bodied, bachelor pad, empty nesters, mature couple, mature individuals, near church, and quiet tenants.*[13]

In light of this and other instances of wasted resources by HUD, Congress should transfer the responsibility for enforcing the Nation's fair housing laws to the civil rights division of the Justice Department where the issue can be handled in the context of comprehensive civil rights enforcement.

Rural Housing Programs

Although the bulk of America's urban and suburban housing assistance is provided through programs administered by HUD, special purpose housing programs are administered by other Departments including Defense, Veterans Affairs and interior, while rural-based housing programs are provided by the Department of Agriculture through the programs of the Farmers Home Administration.

As a consequence of their depression era origins, rural housing programs are markedly different from the suburban/urban programs of HUD, in part reflecting the depression's destruction of large segments of rural America's financial system. Whereas the FHA insured the privately provided mortgages for urban and suburban home buyers, the Farmers Home Administration (FmHA) actually provided the loan, and usually with a significant interest rate subsidy. In addition, whereas a variety of multifamily rental assistance programs are the predominant form of housing assistance provided by HUD to low- and moderate-income urban and suburban households, the FmHA largely provided home ownership assistance, even to rural low-income households by way of deeply subsidized interest rates, in the belief that rental units were not always available in rural settings.

While the emphasis on single-family housing has largely freed FmHA from the major financial fiascoes periodically associated with HUD's multifamily programs, FmHA, in contrast, bleeds from a thousand minor wounds. As GAO studies point out, FmHA programs consistently suffer from high loss and delinquency rates, and have been poorly managed. Loan servicing by FmHA is costly, ineffective, and deficient in timely and accurate information. Recent experience with private servicing of FmHA loans indicates that improved Servicing of $18 billion in loans yielded 5 years savings of $1.2 billion in servicing costs alone. Moreover, better private sector management led to a halving of the delinquency rate and an 80 percent decline in foreclosures.

With the passing of the depression and the re-emergence of private financial institutions in rural America, the low-income assistance responsibilities now attempted by the FmHA should be folded into the new housing block grant program proposed earlier, while the home ownership programs, whether by direct loans or guaranteed loans, should be terminated and replaced by the same FHA programs provided to urban and suburban buyers.

Transition Issues

As noted earlier, any major shift in HUD responsibilities and programs must be coupled with an *orderly* withdrawal from the many long-term commitments and con-

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[13] Perhaps recognizing that the debate within Congress to terminate HUD was serious and that the public ridicule induced by the antics of the Fair Housing staff offered one more reason why the Department should go, HUD, in January 1995 issued a "clarification" which, among other changes, will again permit housing ads to use such terms as master bedroom, great view, Santa Claus, St. Valentine's Day and family room, among others.

tracts HUD has made directly with housing assistance providers—such as developers, nonprofits, local housing authorities—and with the assisted households. Most of the project-based programs involve some form of a long-term contractual commitment by HUD to subsidize some facet of the project such as the interest rate on the mortgage or the rents paid by tenants. In other cases where the commitment is informal, as is the case with public housing, many public housing projects have become dependent on HUD operating subsidies and modernization grants, and their swift withdrawal would have its harshest effect on those least able to bear it—the low-income residents of these projects.

In his *Reinvention Blueprint,* Secretary Cisneros' proposes to deal with this problem by providing vouchers to the tenants of these public housing projects, allowing them to move to better accommodations and forcing the public housing authority to compete with private landlords for the rent money of the assisted households. This is an excellent idea, but with HUD dissolved, this should now become the responsibility of the States and funded out of the block grant they would be receiving.

The tenants in other types of subsidized projects whose contracts are expiring—such as those in Section 8 new construction and renovation—would receive vouchers that they could use to remain in the project, or look elsewhere. Likewise for other types of projects and for those threatening to default on their FHA-insured loan.

Concluding Thoughts

As noted earlier, many of Secretary Cisneros' proposals are commendable, and if enacted and implemented would constitute one of the most significant reforms ever imposed on HUD. As a result, it is tempting for some HUD critics to declare victory, speed up the implementation, and give HUD a second chance. Congress should resist the temptation for two important reasons:

First, from just a budget efficiency standpoint, Congress should recognize that any reforms enacted today can easily be undone tomorrow by another Congress indebted to other interests. By continuing to maintain a "reformed" HUD with most of its project-based programs still intact, albeit at much more modest levels of activity, the seeds of a future expansion remain and would be difficult to stop in a different political environment. But with HUD dissolved and with basic decisionmaking and operations now transferred to the State level, it would be much more difficult, if not impossible, to expand and revive these costly and wasteful programs.

Second, and more important, consolidating HUD resources into a block grant is an integral part of a comprehensive welfare reform program designed to move people into productive self-sufficiency, not to more efficiently inventory the poor by way of large scale custodial programs. With most of its programs purportedly targeted to low- and moderate-income households, HUD is an integral part of toady's welfare system and, thus, must be an integral part of any reform effort.

II

104TH CONGRESS
1ST SESSION

S. 277

To impose comprehensive economic sanctions against Iran.

IN THE SENATE OF THE UNITED STATES

JANUARY 25 (legislative day, JANUARY 10), 1995

Mr. D'AMATO introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

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A BILL

To impose comprehensive economic sanctions against Iran.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Comprehensive Iran Sanctions Act of 1995".

SEC. 2. CONGRESSIONAL FINDINGS.

(a) IRAN'S VIOLATIONS OF HUMAN RIGHTS.—The Congress makes the following findings with respect to Iran's violations of human rights:

(1) As cited by the 1991 United Nations Special Representative on Human Rights, Amnesty International, and the United States Department of

State, the Government of Iran has conducted assassinations outside of Iran, such as that of former Prime Minister Shahpour Bakhtiar for which the Government of France issued arrest warrants for several Iranian governmental officials.

(2) As cited by the 1991 United Nations Special Representative on Human Rights and by Amnesty International, the Government of Iran has conducted revolutionary trials which do not meet internationally recognized standards of fairness or justice. These trials have included such violations as a lack of procedural safeguards, trial times of 5 minutes or less, limited access to defense counsel, forced confessions, and summary executions.

(3) As cited by the 1991 United Nations Special Representative on Human Rights, the Government of Iran systematically represses its Baha'i population. Persecutions of this small religious community include assassinations, arbitrary arrests, electoral prohibitions, and denial of applications for documents such as passports.

(4) As cited by the 1991 United Nations Special Representative on Human Rights, the Government of Iran suppresses opposition to its government. Political organizations such as the Freedom

Movement are banned from parliamentary elections, have their telephones tapped and their mail opened, and are systematically harassed and intimidated.

(5) As cited by the 1991 United Nations Special Representative on Human Rights and Amnesty International, the Government of Iran has failed to recognize the importance of international human rights. This includes suppression of Iranian human rights movements such as the Freedom Movement, lack of cooperation with international human rights organizations such as the International Red Cross, and an overall apathy toward human rights in general. This lack of concern prompted the Special Representative to state in his report that Iran had made "no appreciable progress towards improved compliance with human rights in accordance with the current international instruments".

(6) As cited by Amnesty International, the Government of Iran continues to torture its political prisoners. Torture methods include burns, arbitrary blows, severe beatings, and positions inducing pain.

(b) IRAN'S ACTS OF INTERNATIONAL TERRORISM.—The Congress makes the following findings, based on the records of the Department of State, with respect to Iran's acts of international terrorism:

(1) As cited by the Department of State, the Government of Iran was the greatest supporter of state terrorism in 1992, supporting over 20 terrorist acts, including the bombing of the Israeli Embassy in Buenos Aires that killed 29 people.

(2) As cited by the Department of State, the Government of Iran is a sponsor of radical religious groups that have used terrorism as a tool. These include such groups as Hezballah, HAMAS, the Turkish Islamic Jihad, and the Popular Front for the Liberation of Palestine-General Command (PFLP–GC).

(3) As cited by the Department of State, the Government of Iran has resorted to international terrorism as a means of obtaining political gain. These actions have included not only the assassination of former Prime Minister Bakhitiar, but the death sentence imposed on Salman Rushdie, and the assassination of the leader of the Kurdish Democratic Party of Iran.

(4) As cited by the Department of State and the Vice President's Task Force on Combatting Terrorism, the Government of Iran has long been a proponent of terrorist actions against the United States, beginning with the takeover of the United

States Embassy in Tehran in 1979. Iranian support of extremist groups have led to the following attacks upon the United States as well:

(A) The car bomb attack on the United States Embassy in Beirut killing 49 in 1983 by the Hezballah.

(B) The car bomb attack on the United States Marine Barracks in Beirut killing 241 in 1983 by the Hezballah.

(C) The assassination of American University President in 1984 by the Hezballah.

(D) The kidnapping of all American hostages in Lebanon from 1984–1986 by the Hezballah.

SEC. 3. TRADE EMBARGO.

(a) IN GENERAL.—Except as provided in subsection (c), effective on the date of enactment of this Act, a total trade embargo shall be in force between the United States and Iran.

(b) COVERED TRANSACTIONS.—As part of such embargo the following transactions are prohibited:

(1) Any transaction in the currency exchange of Iran.

(2) The transfer of credit or payments between, by, through, or to any banking institution, to the ex-

tent that such transfers or payments involve any interest of Iran or a national thereof.

(3) The importing from, or exporting to, Iran of currency or securities.

(4) Any acquisition, holding, withholding, use, transfer, withdrawal, transportation, importation or exportation of, or dealing in, or exercising any right, power, or privilege with respect to, or any transaction involving, any property in which Iran or any national thereof has any interest; by any person, or with respect to any property, subject to the jurisdiction of the United States.

(5) The licensing for export to Iran, or for export to any other country for reexport to Iran, by any person subject to the jurisdiction of the United States of any item or technology controlled under the Export Administration Act of 1979, the Arms Export Control Act, or the Atomic Energy Act of 1954.

(6) The importation into the United States of any good or service which is, in whole or in part, grown, produced, manufactured, extracted, or processed in Iran.

(c) EXTRATERRITORIAL APPLICATION.—In addition to the transactions described in subsection (b), the trade

embargo imposed by this Act prohibits any transaction described in paragraphs (1) through (4) of that subsection when engaged in by a United States national abroad.

(d) EXCEPTIONS.—This section shall not apply to any transaction involving the furnishing, for humanitarian purposes, of food, clothing, medicine, or medical supplies, instruments, or equipment to Iran or to any national thereof.

(e) PENALTIES.—Any person who violates this section or any license, order, or regulation issued under this section shall be subject to the same penalties as are applicable under section 206 of the International Emergency Economic Powers Act (50 U.S.C. 1705) to violations of licenses, orders, or regulations under that Act.

(f) APPLICATION TO EXISTING LAW.—This section shall apply notwithstanding any other provision of law or international agreement.

SEC. 4. OPPOSITION TO MULTILATERAL ASSISTANCE.

(a) INTERNATIONAL FINANCIAL INSTITUTIONS.—(1) The Secretary of the Treasury shall instruct the United States executive director of each international financial institution described in paragraph (2) to oppose and vote against any extension of credit or other financial assistance by that institution to Iran.

(2) The international financial institutions referred to in paragraph (1) are the International Bank for Reconstruction and Development, the International Development Association, the Asian Development Bank, and the International Monetary Fund.

(b) UNITED NATIONS.—It is the sense of the Congress that the United States Permanent Representative to the United Nations should oppose and vote against the provision of any assistance by the United Nations or any of its specialized agencies to Iran.

SEC. 5. WAIVER AUTHORITY.

The provisions of sections 3 and 4 shall not apply if the President determines and certifies to the appropriate congressional committees that Iran—

(1) has substantially improved its adherence to internationally recognized standards of human rights;

(2) has ceased its efforts to acquire a nuclear explosive device; and

(3) has ceased support for acts of international terrorism.

SEC. 6. REPORT REQUIRED.

Beginning 60 days after the date of enactment of this Act, and every 90 days thereafter, the President shall sub-

mit to the appropriate congressional committees a report describing—

(1) the nuclear and other military capabilities of Iran; and

(2) the support, if any, provided by Iran for acts of international terrorism.

SEC. 7. DEFINITIONS.

For purposes of this Act—

(1) the term "act of international terrorism" means an act—

(A) which is violent or dangerous to human life and that is a violation of the criminal laws of the United States or of any State or that would be a criminal violation if committed within the jurisdiction of the United States or any State; and

(B) which appears to be intended—

(i) to intimidate or coerce a civilian population;

(ii) to influence the policy of a government by intimidation or coercion; or

(iii) to affect the conduct of a government by assassination or kidnapping.

(2) the term "appropriate congressional committees" means the Committee on Foreign Relations

of the Senate and the Committee on International Relations of the House of Representatives;

(3) the term "Iran" includes any agency or instrumentality of Iran;

(4) the term "United States" means the several States, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, the Virgin Islands, and any other territory or possession of the United States; and

(5) the term "United States national" means—

(A) a natural person who is a citizen of the United States or who owes permanent allegiance to the United States;

(B) a corporation or other legal entity which is organized under the laws of the United States, any State or territory thereof, or the District of Columbia, if natural persons who are nationals of the United States own, directly or indirectly, more than 50 percent of the outstanding capital stock or other beneficial interest in such legal entity; and

(C) any foreign subsidiary of a corporation or other legal entity described in subparagraph (B).

O

U. S. Department of Housing and Urban Development
Washington, D C. 20410-4500

OFFICE OF INSPECTOR GENERAL

March 30, 1995

Honorable John F. Kerry
Ranking Minority Member
Subcommittee on Housing Opportunity
and Community Development
Committee on Banking, Housing and Urban Affairs
United States Senate
SR-421 Russell Senate Office Building
Washington, DC 20510-2102

Dear Senator Kerry:

As a follow-up to your request during the March 14, 1995 hearing on the "Direction of Housing and Community Development Policy," I am enclosing a list of 34 statutory and administrative actions which the U.S. Department of Housing and Urban Development (HUD) Office of Inspector General believes should be taken now to improve HUD's program execution. This list is being submitted for the hearing record.

We appreciate your continued efforts to improve the important program delivery of HUD. Should you or your staff have any questions, or need any further assistance from our office, please contact me on (202) 708-0430.

Sincerely,

Susan Gaffney

Susan Gaffney
Inspector General

Enclosure

HUD/OIG SUGGESTED ACTIONS FOR IMPROVING HUD'S EXISTING PROGRAM DELIVERY

Interim Legislative Changes

Congress should immediately enact the following changes to existing statutes to relieve HUD from requirements which hinder the effective delivery of its programs. These items are generally in keeping with HUD's Reinvention Blueprint objectives, and for the most part there is a growing Congressional consensus that these changes should be made. Therefore, they should not await the outcome of the larger debates on major HUD program restructuring, or whether we need a separate HUD type agency.

Multifamily Housing Programs: Project Based Assistance

1. Congress should repeal the Loan Management Set Aside program to discontinue HUD's "propping up" of distressed projects, as has been the practice in the past. [Section 8(v) of the United States Housing Act (USHA) of 1937]

2. HUD should be given maximum flexibility in renewing project-based subsidy contracts, including:

   - authority to convert project-based assistance to tenant-based assistance when it is deemed necessary to better serve tenant interests, and

   - authority to discontinue subsidizing rents far in excess of rents for comparable unassisted units in the same locality.

   This new flexibility could be used as thousands of contracts with private owners come due over the next several years. Reducing rents to just the level of the Fair Market Rents could serve as a catalyst for owners to refinance or take other cost saving measures. The subsidy savings could be somewhat offset by FHA insurance fund losses for projects that default/foreclose because of the reduced rents, but the long term savings could be enormous. [Section 8(c)(2)(C) of the USHA of 1937, as amended by 142(d) of the Housing and Community Development Act (HCDA) of 1987]

3. Congress should repeal the Title 2 and Title 6 Prepayment/Preservation Programs and replace them with a more reasoned and balanced approach for preserving/providing housing for tenants of these projects. This would enable HUD to discontinue paying owners windfall profits for projects that threaten to prepay their mortgages and remove the low income character of the units. The current

programs, which potentially involve about 400,000 Section 8 units, have been characterized by our office as "scandals" and "taxpayer rip offs." Our April 1994 audit of the Title 6 Program estimated that a more flexible approach to preserving units could save tens of billions of dollars. [Low-Income Housing Preservation and Resident Homeownership Act (LIHPRHA) of 1990]

4. HUD should be relieved from the need to over subsidize projects sold through HUD property disposition programs. Well intentioned but ill-advised laws prevent FHA from operating in a business-like fashion. Last year, the Congress and HUD took some steps to improve this situation, but more needs to be done to assure that HUD staff have maximum flexibility in attempting to dispose of properties in a cost effective and timely manner. [Section 203(e),(f),(g) and (h) of the HCDA of 1978 and the Multifamily Property Disposition Act of 1994]

5. Congress should change existing program enforcement and bankruptcy laws which serve to protect bad project owners over HUD program interests. Changes should give HUD the ability to pursue the assets of project partners in equity skimming or asset diversion cases, as well as provide an exemption to the automatic stay provisions of the Bankruptcy Code for HUD's multifamily program activity.

<u>Public and Indian Housing Programs</u>

6. Congress should strengthen HUD's statutory PHA takeover authority to enable HUD to bypass court ordered receiverships and install its own form of receivership when there is an imminent or existing threat to the health, safety or well being of PHA residents. Such authority should include the ability to abrogate State or local laws or contracts governing PHA operations when the PHA is in substantial breach of their Annual Contributions Contract (ACC) with HUD, as well as the ability to take possession, demolish, transfer or sell the housing stock of such PHAs. [Section 6(j) of the USHA of 1937]

7. Congress should enable HUD to discontinue paying operating subsidies on long term vacant units. Approximately 112,000 units nationwide are vacant and many are boarded up with little hope of getting on line in the near future. Yet, HUD continues to pay an estimated $235 million a year in operating subsidies on these vacant units. [Section 9 of the USHA of 1937]

8. Congress should repeal provisions that insist that every single unit of public housing removed from the stock needs to be replaced on a "one for one" basis. This current

restriction creates numerous situations where otherwise more cost effective measures, such as demolishing badly deteriorated units, are deferred because replacement units are not immediately available. Flexibility needs to be given to the PHAs in such situations. [Section 18 of the USHA of 1937]

9. Congress should relieve HUD and PHAs of strict preference rules [Sections 6(e)(4)(A) and 8(d)(1)(A) of the USHA of 1937], and rent setting and admission policies [Section 3 of the USHA of 1937], as a means to increase both the rental income stream and the resident income mix at projects. Operating subsidies could be reduced substantially if the tenant portion of rent payments were increased through these measures.

10. Congress should discontinue HUD's role in attempting to regulate and fund the testing and abatement of lead based paint. HUD has demonstrated neither the capacity nor the administrative capability to perform these functions. The EPA should be designated as the sole Federal agency for reducing the hazards associated with lead paint as well as other lead contaminated products. [Lead-Based Poisoning Prevention Act, 42 U.S.C. 4821-4526 and 24 CFR Part 35]

CPD Homeless Programs

11. In accordance with current CPD initiatives, and the HUD Reinvention Blueprint, legislation should be passed to consolidate HUD's homeless programs into one block grant program. This will alleviate administrative burdens and provide greater program flexibility to meet local program needs. [Stewart B. McKinney Homeless Assistance Act of 1987]

Addressing Most Critical Program Needs Now

In addition to the above statutory relief from Congress, HUD needs to take immediate aggressive action to address the small number of severely distressed multifamily and public housing projects which tend to taint the entire agency and all of its program efforts. This would send a message to the Congress and the public that HUD can change and is capable of carrying out the most difficult aspects of its Reinvention Blueprint. Our suggestions in these areas follow. While we acknowledge that many of these actions are currently being pursued to varying degrees, there is a need to better focus, support and ensure progress on these items as the highest priorities of HUD's Principal Staff.

Multifamily Housing Programs - HUD should take the following actions to accelerate efforts to address significant problems in

its multifamily housing program portfolio.

12. HUD needs to fully utilize and test its existing staff capacity for handling the below noted multifamily housing program tasks by setting and adhering to aggressive goals for all headquarters and field staff units. While longer term systemic program improvements are being pursued by headquarters staff, field operations should be empowered and challenged to use existing program resources, tools and enforcement powers to take on the most troubled projects known in their respective jurisdictions.

13. HUD needs to develop and implement a procurement plan for acquiring the outside expertise and resources needed to assist in the timely and successful pursuit of the below noted actions to improve HUD's multifamily housing program delivery.

14. HUD needs to immediately refine its project information systems to:

    - provide early problem warning signs for targeting a greater emphasis on preventative measures to deter defaults and prevent properties from becoming troubled, and

    - identify the universe of troubled multifamily properties, and their financial and operating profiles, to enable HUD to make more informed and timely decisions to correct or minimize problems.

15. HUD should immediately begin to assess the costs and benefits of its programs for assisting troubled properties so it can make informed decisions on the kinds of assistance that should be used and when such assistance should be triggered.

16. HUD should base all decisions on continuing assistance to multifamily properties, whether such assistance is in the nature of prepayment/preservation incentives or the renewal of Section 8 contracts, on comprehensive physical, financial, and economic analyses of properties. Decisions should only be made under terms which are favorable to the Department, including flexibility to adjust rents to comparable market rents.

17. HUD needs to take action to stop the unwarranted escalation in Section 8 contract rent increases, through either rent comparability reviews or other means, such as a cost-based measure being developed by HUD.

18. HUD should immediately begin to apply project reserve funds, when feasible, to meet increased owners' costs, rather than automatically granting contract rent increases to such owners.

19. HUD should evaluate and modify its systems for compensating property owners and their management agents to provide incentives for improving the efficiency of property management. HUD should also accelerate transfers of ownership and encourage the use of nonprofit organizations where appropriate.

20. HUD should continue its mortgage sales efforts as a means of alleviating the servicing burdens on HUD, and reenergizing project ownership and management.

21. HUD needs to get tough and more aggressively use its existing enforcement tools to deter and sanction the gross mismanagement of insured/assisted properties. This will require overcoming HUD's past culture which had a wholesale disregard for available enforcement tools. The key to such a culture change is the need to make the sanctions impact the owners and agents, not the tenants or the Department. Equity skimming by owners and agents rob the tenants of quality housing and contribute to HUD losses through default and foreclosure. A sound enforcement program could save HUD millions of dollars, and improve tenant living conditions.

Public Housing and Section 8 Tenant-Based Assistance

22. HUD should act aggressively and decisively in dealing with large troubled public housing agencies (PHAs). HUD should assess the current status of large troubled PHAs as well as their past history. Sanctions should be taken immediately, including HUD-initiated receivership and the use of private management companies, where warranted. Unobligated funding should be recaptured when HUD has good cause to believe that the funds will be misspent or will not directly benefit the PHA's residents. If feasible, HUD should discontinue its project-based assistance to certain troubled "developments," and instead, residents should be given portable certificates or vouchers.

23. HUD should immediately begin to assess the public housing stock, both physically and operationally, as a basis for determining the most cost effective and beneficial way of assisting developments now and in the future. On the basis of these assessments, HUD should determine if certain developments should be retained or deprogrammed (through demolition or disposition). If retained, HUD should identify other less costly and potentially more effective funding alternatives.

24. HUD should act aggressively to deregulate and decontrol non-troubled public housing. Major deregulation efforts should occur with respect to tenant eligibility, applicant screening, admissions, resident mix, household-income determinations, lease/grievance procedures, property standards, project development, and utility allowances.

25. HUD, HHS, PHAs, localities, and local providers should work closely to strengthen and improve welfare-to-work efforts in public housing. HUD should begin immediately to facilitate the conversion of public housing to transitional housing.

26. HUD should lower maximum Section 8 Fair Market rents (FMRs) from the 45th percentile of all rental housing in the locality to the 40th percentile. This would save about $300 million.

27. HUD should end PHAs' monopoly on the administration of Section 8 vouchers and certificates and open these programs to competition. This could reduce the costs of administering these programs and perhaps even result in improving program administration.

28. HUD needs to fully utilize and test its staff capacity for handling the above public housing program tasks by setting and adhering to aggressive goals for all field and headquarters operating units.

29. HUD needs to develop and implement a procurement plan for acquiring the outside expertise and resources needed to assist in the transformation of troubled public housing authorities.

Steps Towards the HUD Reinvention Blueprint

30. Performance Measurement - HUD should expedite the design and development of performance measures and related data collection and reporting systems for the proposed 3 performance-based funds and the Federal Housing Corporation. Even if HUD's Blueprint isn't enacted by Congress, the results of this effort will still serve as a basis for improving the delivery of the existing CDBG, HOME, Section 8 and FHA programs.

31. Rulemaking Reforms - HUD should immediately move to stop the proliferation of extensive rules in its programs. The public rulemaking process should be curtailed where statutory intent is clear, or where statutory requirements can be carried out through contractual terms and conditions without time consuming and less flexible rulemaking processes. OMB's consent is needed to empower HUD in this

regard. Such efforts will not only ease the regulatory burden on HUD and existing program participants, but they will pave the way for a smoother transition to Blueprint objectives for a less prescriptive, compliance oriented Federal program environment, in favor of locally driven program processes which are measured by actual outcomes and benefits.

32. Automated Systems - Automated systems are critical to producing program information essential for carrying out HUD's new oversight role for the performance-based funds proposed in the Blueprint. Since CPD is in process of developing a new system to cover the information needs of the existing CDBG, HOME, ESG and Shelter Plus Care programs, management should assure that this new system development effort can also serve as the basis for the systems needs of the COF and AHF programs proposed in the Blueprint, as well as other existing HUD grant programs. Relatedly, we believe that CPD's consolidated program planning efforts are moving well in the direction of the Blueprint. However, these and other HUD program area systems efforts increase the need for a strong Departmentwide "information management function." We also believe strong management action is needed to correct longstanding systems security weaknesses as we enter a high risk downsizing environment.

Improving HUD's Program Management

33. Balanced Program Management - The Secretary and his Principal Staff need to assure that their actions are consistent with their stated strategies and objectives. In all matters, management needs to responsibly assure that its program policy proposals and decisions are made in the context of HUD's administrative capacity. Failure to balance HUD's program mission objectives with HUD's operational capacity could undermine a successful implementation of HUD's Blueprint or other change options.

34. Organizational Streamlining - HUD needs to complete its field reorganization and expedite the planning and implementation of a headquarters reorganization in a manner which will both serve to streamline HUD's existing program delivery and form a basis for moving towards the Reinvention Blueprint with minimal change. In the long term, the empowerment of HUD's field operations can eliminate or reduce many headquarters oversight and staff functions in HUD's respective program areas. The number and location of HUD field operating units should be based on programmatic need, cost-benefit, and capacity analyses, not political reasons.

REINVENTION OF HUD AND REDIRECTION OF HOUSING POLICY

WEDNESDAY, MARCH 29, 1995

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING OPPORTUNITY AND
COMMUNITY DEVELOPMENT, AND
SUBCOMMITTEE ON HUD OVERSIGHT AND STRUCTURE,
Washington, DC.

The Subcommittees met at 10:02 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Connie Mack (Chairman of the Subcommittee on Housing Opportunity and Community Development) and Senator Lauch Faircloth (Chairman of the Subcommittee on HUD Oversight and Structure) presiding.

OPENING COMMENTS OF SENATOR MACK

Senator MACK. The hearing will come to order.

Just to give everybody kind of a sense of the time constraints, we have a vote called for 10:45. I don't know how many of my colleagues are going to be joining us and how long opening statements might have to be.

I would encourage them to be brief so that we can get to the testimony of the Secretary.

I want to welcome everyone to the second joint hearing of the Housing Opportunity and Community Development Subcommittee and Senator Faircloth's HUD Oversight and Structure Subcommittee.

Today, we will continue to look at how we can best provide America's families the housing opportunities they deserve and the tools that will empower them to achieve independence and home ownership.

Having reviewed the latest version of the Department's "Blueprint for Reinvention," I intend to ask some serious questions about how and whether it will work.

I want to be very clear. We must confront the many problems that trouble so many public housing communities in this country. Too often our policies and programs, no matter how well-intentioned, are hurting the very communities and families they are supposed to be helping.

No one needs to be reminded of the crime and violence, the drugs and guns, the family breakdown that affects so many of our public housing residents.

I believe serious and effective reform starts with setting objectives and then finding ways to reach them. The goal of housing pol-

icy should be to empower America's families to achieve their own aspirations of independence and home ownership.

With that goal in mind, we must develop policies and programs that accomplish our objectives without creating the kind of family and social breakdown fostered by many of our current efforts.

While we should take seriously any proposal to make HUD more effective and more taxpayer-friendly, I question whether HUD's "Blueprint" represents such a reform. I'm afraid it has more to do with changing names and faces in some of the programs at HUD than it does with providing hope and opportunity for ordinary Americans.

The Blueprint leaves many questions unanswered. For example:

Is HUD willing and able to return control and accountability to State and local agencies that are closer to the people and allow those entities to operate without excessive Federal intervention, or is the Blueprint creating new opportunities for micromanaging these programs?

Since the Blueprint has changed from its original version, what is the pace and process for the transition HUD will make under the new version? How will this impact the people HUD is trying to serve with this reform?

What are the consequences of creating a Government-owned Federal Housing Corporation? How would this change affect the programs that insure single-family mortgages for low- and moderate-income families as well as affordable multifamily housing developments?

What are the cost implications of restructuring HUD's multifamily housing portfolio?

Finally, how will the operative details of the Blueprint be achieved in a climate of shrinking staff resources?

Let me now welcome Secretary Cisneros to what I hope will be the first of many appearances before our Subcommittee. I know the Secretary brings a deep passion to the job of trying to improve the well-being of our communities and the people who live in them.

We look forward to hearing more about the Blueprint, Mr. Secretary.

We are also pleased to welcome a panel of distinguished mayors: Mayor Stephen Goldsmith of Indianapolis; Mayor Bret Schundler of Jersey City; and Mayor Dennis Archer of Detroit.

We look forward to hearing your views on the role of cities in meeting our Nation's housing and community needs.

I now turn to Senator Kerry for his opening statement.

OPENING STATEMENT OF SENATOR KERRY

Senator KERRY. Mr. Chairman, thank you very much.

I'm going to do exactly what you've requested and really not make an opening statement. I think I made a long one at the last hearing and that will serve as a broad guideline for how I intend to approach these hearings.

But I do want to welcome the Secretary and the mayors here. We want to take advantage of this opportunity to explore not just your proposals for change, but also some of the others that are on the table and to really try to examine what works.

The only comment I would make is that I again reiterate. I think we have to be very, very careful to take into full account the 60 or so years of experience now that we have with housing and to measure very carefully what works, what doesn't, not to throw out the good in the effort to make a cure here of the bad, and to really think very carefully about the implications of the market and how the market really works when left to its own device with respect to housing.

I think it's fair to say that it has not always been a benign arena and there is nothing to suggest that our wishes to do away with the ills of HUD are automatically going to make it benign in this age.

There are certain laws of supply and demand and other aspects of the market which have made it very tough for people of low income to be able to get adequate housing.

So my prayer is that we will take what works and legitimately change what doesn't.

Thank you, Mr. Chairman.

Senator MACK. Thank you.

Senator Faircloth.

OPENING STATEMENT OF SENATOR FAIRCLOTH

Senator FAIRCLOTH. Thank you, Senator Mack. And I want to welcome Secretary Cisneros to the Committee.

This is the second of what I'm sure will be many hearings examining the role of HUD and its future.

Mr. Chairman, it is no secret that I want to abolish HUD. I have introduced legislation to do so. Since HUD was created in 1965, I think it has failed to accomplish what it set out to do, which is help our cities promote home ownership.

I question whether America and its cities are better off because we have had HUD for the last 30 years, particularly given what HUD has spent.

As you can see from this chart, HUD's spending has been on a steady increase since the day it started. HUD's spending increases will continue into the next century. Frankly, I don't know if America can afford not to abolish HUD.

HUD has unused budget authority of nearly $192 billion now.

Today, Secretary Cisneros is going to discuss his Reinvention Blueprint for HUD. But regardless of how hard he works at it and how much he has devoted to it, I don't think HUD can be reinvented. Even under the Blueprint, HUD's spending will increase by $11 billion over the next 5 years.

When I read his plan, I'm reminded that the new HUD looks very much like the old HUD. The plan calls for rolling HUD's 240 programs into three block grants. In looking at the proposal, I think HUD will be micromanaging communities that will have to submit consolidated plans in order to win funds from HUD.

I think we should have one housing and urban development grant for the States. And this is not in any way taken to mean that I don't believe we should help those less fortunate with public housing or help them to have housing. But I believe that North Carolina knows what is best for North Carolina and Florida knows what's best for Florida or Massachusetts for Massachusetts.

We don't need an overwhelming bureaucracy in Washington, and HUD has some 11,000 employees. Of course they're not all in Washington. But we don't need a bureaucracy here telling local communities how to create jobs or to house people.

Given the track record of HUD, they are the last people who should be talking about revitalizing communities.

Mr. Chairman, my concern is that if we don't abolish HUD, if we simply try to reinvent it, we will be having this same discussion 5 years from now.

HUD will fail again. Our cities will not be better off.

I am sure the number of block grants will go from 3 to 60 and we'll be right back where we started and where we are now.

With that, Mr. Chairman, I conclude and look forward to the testimony.

Senator MACK. Senator Moseley-Braun.

OPENING STATEMENT OF SENATOR MOSELEY-BRAUN

Senator MOSELEY-BRAUN. Thank you very much, Mr. Chairman for holding the second hearing on the Reorganization of HUD.

I believe the future of this agency is a critical issue in this country and to all Americans, and I hope that there is a future for this agency and I frankly welcome the opportunity to discuss the direction that this agency will take.

At the outset, Mr. Chairman, I must point out that I'm very disturbed by the size of the cuts and the scope of the cuts in HUD programs and rescissions bill passed by the House and the Senate Appropriations Committees.

The Senate version does provide some relief from the draconian House bill and I'm very happy to see that funding has been restored for the Community Development Block Grant, for the public housing subsidies, and housing opportunities for persons with AIDS.

But the reductions, frankly, are still at damaging levels. They completely undermine the public housing modernization program, community development initiatives, and will undermine current efforts at restructuring and revitalizing this important agency.

As we begin to consider this bill today in the Senate,

I hope we can restore some of the funding.

HUD was created to implement the Government's commitment to assist with economic growth and to create opportunities in distressed communities. HUD was also created to provide a vehicle for this country's affordable housing program for all Americans.

I hope that the Members of the Committee will continue to address the issues before us in this spirit and that we will not retrench from that commitment.

The creation of HUD in 1965 solidified this Nation's mission in revitalizing our urban areas. Our cities serve as a crux to economic growth for the entire country. The policies of the past have not always supported urban areas. This has resulted in many neighborhoods and communities being, frankly, cordoned off from jobs and economic opportunities.

The need for the Federal Government's role in encouraging economic growth in our urban centers is greater now than ever.

We must also ensure that this country does not take a step backward in providing decent and affordable housing, as well as provide for vulnerable populations in this country.

Since the passage of the National Housing Act in 1934, the FHA has made home ownership a reality for millions of Americans.

In 1949, the housing act provided that, and I quote:

> The goal of a decent home and suitable living environment for every American family is reachable.

I believe that it is still reachable. I believe that we must not retrench from that goal.

The bill also provided for grants to local governments for community planning. Many of our public housing and subsidized housing programs have also provided shelter for millions of families, senior citizens, as well as independent living for the disabled.

More recently, HUD has provided funding to help house persons with HIV AIDS who face unique and severe challenges in their housing needs, and this agency has set out to help that population as well.

While Congress continues to address the housing needs of Americans, the deteriorating state of the housing stock in the country and the needs of our cities, again, we cannot retrench on the commitments that were made in the housing acts going back some 60 years now.

At the same time, even as we face not retrenching, as we face the challenge of going forward and revitalizing and reforming this agency, we must acknowledge, frankly, the failures of the agency. We must reject the top-down, bureaucratic approaches that tell local authorities what's right and what works in their communities. We must help put an end to housing policies that do not provide work incentives or discourage the notion that subsidized housing was intended to provide for temporary shelter.

I look forward to working with the Secretary. I look forward to the Secretary's testimony on the HUD Blueprint for Reform.

I know that he has worked long and hard at reforming the bureaucracy and he has worked long and hard at providing for performance goals and accountability at this agency.

I believe, Mr. Chairman, that that is the direction that we ought to take, renewing our commitment to provide for decent housing for all Americans and reforming the agency that was set up to achieve that goal and supporting efforts to provide for the accountability and provide for the performance that we all have a right to expect from this agency of the Government.

I therefore want to again commend you for holding this hearing and commend the Subcommittees and suggest to you that I look forward to working toward a solution to the many problems that HUD faces, without losing sight at the same time of the goals that I believe as Americans we have a right to expect that our government will continue to support.

Senator MACK. I want to welcome Senator D'Amato, Chairman of the Full Banking Committee to today's hearing.

Do you have an opening statement that you would like to make?

OPENING COMMENTS OF SENATOR D'AMATO

Senator D'AMATO. Well, first of all, I want to commend you, Chairman Mack, and Chairman Faircloth for this joint Subcommittee hearing.

And in the interest of time, I'm going to ask that my full remarks be published in the record as if read in their entirety.

This process is absolutely essential. I am certain that the work that you have undertaken will produce not only legislative change and regulatory reform, but the kind of product that will bring about needed changes in HUD.

The problems have been systemic. I think that the Secretary has brought about some changes that are important and it is absolutely critical and essential that we help in this process, shape this process.

I am encouraged by the tough position that Senator Bond has taken in terms of saying and mapping out very clearly that we cannot just continue to spend and spend without regard to where the dollars are going to come from.

He's been rather courageous in this. And I think it's important for us to not kid the people and put a whole bunch of programs out there that look good, but, yet, we don't have the ability to pay for.

So, I think it's important that this Committee does this kind of work, and I want to congratulate you and Senator Faircloth and the members of this Committee.

Senator MACK. Thank you.

Senator Sarbanes.

OPENING STATEMENT OF SENATOR SARBANES

Senator SARBANES. Thank you very much, Mr. Chairman, for calling this hearing today, continuing the series of hearings on proposals for restructuring the Department of Housing and Urban Development.

As always, I'm pleased to have Secretary Cisneros here before the Committee and I join others in welcoming him here.

He took on a very tough job, I must say, as this Committee well knows, since the Department had been racked by a number of scandals in the 1980's. And Secretary Kemp, I thought, sought to address those, but it, in a sense, immobilized them from the rest of the agenda, since they faced such a difficult problem in terms of cleaning up the situation which he found, to which, of course, he was very much committed.

We've tried to work with the Department to address its management problems. Last year, of course, this Committee passed the Multifamily Housing Property Disposition Reform Act, which gave the Department some very important tools. And we also in the reauthorization bill we reported out, but which then did not pass on the floor for other reasons, I think, not the substance of the bill, we tried to address a number of continuing problems.

I think it's clear from this Committee's past work that responsible reform will include several components which I think are reflected in HUD's Blueprint. We need to consolidate programs in order to lessen the workload.

I feel very strongly we need to move more aggressively to stabilize the troubled housing inventory.

There is a housing inventory out there, and for most of it, it makes real sense in terms of cost to find ways to stabilize it and not to lose it.

We also need to work at making some of HUD's programs more cost effective.

I think last year we took a balance approach on these reform principles. We need obviously to correct the deficiencies and at the same time strengthen the core programs that are working to revitalize communities, provide affordable housing, and promote home ownership.

Last year, as you recall, we consolidated the homeless in the rental assistance areas. We reformed the rent structure in public housing, which I thought was a very important step.

We gave increased enforcement tools to HUD to get at bad housing managers to make the severely distressed public housing programs more workable.

In closing, let me just underscore two points.

One is I'm very concerned about some of the rescissions that we are confronting which were very heavy in the housing area, clearly disproportionately so.

Actually, I think there's a problem in how things are grouped within the Appropriations Subcommittee. The money that was needed was FEMA money for disaster assistance, and of course, the money came out of other agencies grouped within that Subcommittee in the Appropriations Committee, in a sense, just by chance.

It seems to me clear that the disaster relief money ought to sort of come from across the board, if you're not going to declare it an emergency and proceed with it.

Finally, let me urge my colleagues to take a second look at the HOME program as an important example for HUD reforms. It was the bipartisan Cranston–D'Amato task force that conceived of the HOME program. It builds on a partnership between Federal, State, and local governments, for-profit and not-for-profit sectors. It provides a lot of flexibility to meet local needs and to fill financing gaps.

HOME is now working to build State and local capacity in low-income housing that does not uniformly exist.

It's actually managed through an information system that allows the Federal Government to track progress and results on a day-to-day basis, and I think the results thus far have been very good, indeed. And we need to continue to build on that program.

I'm hopeful that out of the hearings, we can evolve a responsible and bipartisan effort to reform HUD and I look forward to working with the Secretary and the other Members of the Committee to try to achieve that.

Thank you very much.

Senator MACK. Thank you.

Mr. Secretary.

STATEMENT OF HENRY G. CISNEROS, SECRETARY, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, WASHINGTON, DC.

Mr. CISNEROS. Thank you very much, Mr. Chairman.

Mr. Chairman, Senators, first of all, let me say how much I appreciate the opportunity to present because today is not just another Senate hearing. This is really the fundamental breakthrough opportunity for this Department.

What we've done over the last several years is get in position to make change, and we've done it consistently.

But in the course of the last three or four months, we have done what we think is a sincere job of offering up a way that together, between the Executive and the Congress, that we can create a new organization, not only because we know we have to downsize and not only because we know we have to simplify, but most importantly, because we must do a better job in America's communities.

I believe that the outline of the plan that we have presented, together with the input that we get from you, can result in an organization that can meet the pressing needs of people who live in America's cities and communities across America.

So we offer this in the sense of the beginning of a work session, the beginning of a dialogue, that I believe can have profound impact for those who live in America's communities.

As a result, this is a command performance in many ways and we have a substantial number of our team from HUD here. I'd like to quickly introduce them. They're people who have been confirmed by this Committee. But I want you to know that they're doing an outstanding job.

The Deputy Secretary of the Department who is Acting Deputy Secretary at this point. He will be here for confirmation in short order. Dwight Robinson is seated on the front row.

He's joined by the Assistant Secretary for Housing——

Senator MACK. Since we're going to go through this——

Mr. CISNEROS. The Assistant Secretary for Housing, Nic Retsinas, the head of FHA, has some of the most pressing problems that HUD confronts in his responsibility.

Assistant Secretary Roberta Achtenberg, who works on fair housing issues.

The Assistant Secretary for Policy Development and Research, Mike Stegman, who has been very key to our work.

The General Counsel, Nelson Diaz.

The Chief of Staff of the Department, Bruce Katz.

In the spirit of a command performance, Mr. Chairman I have the good fortune on a personal note of having my daughter here from spring break with her college roommate. She's accompanied by my wife today.

So I'd like to ask my daughter Mercedes, her friend Lisa Montoya, and my wife Mary Alice, if they could please stand and be recognized.

It's a special pleasure to be part of a hearing that includes three distinguished mayors, all of whose cities I've had the opportunity to visit at some point or the other—Mayor Archer, Mayor Schundler, and Mayor Goldsmith. And I look forward to hearing their testimony as well.

Senators what we are proposing is a three-part reinvention of the Department. At the conclusion of our work, jointly, the Executive's proposals, the Congress's treatment of them, this Department will not be the same place.

It will be vastly smaller, greatly simplified, with market discipline infused into its work and a clear sense of mission and goals redefined.

The three elements of reinvention are, first, dramatic consolidation.

Second, a fundamental transformation of public housing as we know it in the United States today.

Third, the creation of a Federal housing corporation, not a government bureaucracy as usual, but a corporation that is substantially leaner and that has as its fundamental purpose to increase home ownership rates to all time highs in the United States by the end of the century.

We believe that that is achievable.

Consolidation, the first element of our plan, is a key element throughout.

I have provided a chart which you should have in front of you that is broken into the three sections of our analysis—consolidation, public housing, and FHA.

It doesn't follow exactly the points of my testimony, but if you will turn to page 1, the third actual leaf of the document, you will see how our consolidation proposal works.

We're consolidating 60 separately funded specialized programs into three funds. In addition, some other 200 programs of this Department, a hodge-podge of active programs, inactive programs, set-aside, technical assistance, eligible activities, regulatory functions, insurance authorities, are consolidated.

The bottom line is three funds.

First, as you can see on the far right-hand column of the chart, a community opportunity fund which essentially builds on the existing community development block grant program, which many of you know, it has 20 years of success, one of the most successful urban programs that we have, that will fund communities on a ratio of 70 percent to localities and 30 percent to States.

I trust all of you have this in front of you and you don't have to look on with one another. If not, we have copies that we can distribute.

The first of these is the community opportunity fund. You see it in the middle of that right-hand column. And as I say, it builds on the Community Development Block Grant program. But as you will see from the next page of the document, you can see what other programs are put together.

Now some will say that that is not dramatic change. But to communities that have been using these different programs, having to apply for different titles, with different deadlines, with different bureaucracies, each of which is backed by an office somewhere, to put all of those in one place where communities can compete for economic development opportunities is very profound.

The second is the affordable housing fund. You see it at the bottom of the right-hand column. It too is a consolidation of numerous programs listed on page 3.

These are some of our largest programs. They are again individually applied for today, competitive nationally, and they will be assembled into a very substantial fund for affordable housing development.

Now some have questioned whether we ought to have just one fund instead of an economic development fund and an affordable housing fund. But those are discrete functions that communities handle in different ways and it's why we have subdivided them into two different funds.

In addition, you will see a housing certificates fund. But I will say more about that later since it supports our public housing reinvention.

Let me just mention some of the highlights of the consolidation effort.

First of all, consolidation puts together overlapping competitive programs into consolidated funds which in and of itself is infinitely simpler for the bureaucracy but clearly simpler for communities.

It also is set up in a way that we simplify the planning process in communities. Instead of communities having to submit multiple plans and multiple applications, we're calling for a consolidated plan, one plan, simpler than the hodge-podge that exists today.

If communities set forth what they want to do with the funds, the funds are provided on a formula basis and it should work much better.

You'll hear from the mayors on the general principles, I think, of that concept.

In addition, we are supporting the work of the community development corporation, some 3000 community development groups we work with, and so we're directing 30 percent of the affordable housing fund will go to nonprofit community development organizations, some national groups, some community-based groups, but nonprofits.

One very important aspect of this consolidation is the concept of setting up bonus funds.

We will set aside some of the money at 10 percent in the case of the affordable housing fund, about $250 million in the case of the community opportunity fund.

For the first time, instead of using sanctions and threats of ending funds, communities compete for a bonus pool. We think that the infusion of that dimension, that if they accomplish what they have said that they want to accomplish, and then can compete for additional funds, infuses a level of positive competition that we see in the private sector, but rarely works in Government programs.

This will not occur all in the course of one year. As you can see from the chart, the initial chart, we have an interim period in which we block up, and the reason is because several of these funds need to strengthen their legs.

Our homeless programs, the consolidation from six different McKinney programs, to one, will require a little time to make sure the homeless programs work.

Similarly, our programs for persons with AIDS.

Our Native American programs is another instance where we try to consolidate programs under a Native American title, very importantly.

Let me just say to make a point that Senator Faircloth mentioned earlier about whether or not these funds really ought to be consolidated far more and go to the States.

We believe strongly that the formulas that we've established, 70 percent of CDBG goes to cities, 30 percent goes to the States for the small communities. Sixty percent of the HOME program, which Senator Sarbanes mentioned, goes to cities, 40 percent goes to the States—work very well. They're time-tested and as a result, we feel very strongly that they can work.

The second major element of our reinvention is the transformation of the public housing system.

No aspect of our reinvention is more controversial or far-reaching or, for that matter, more exciting.

What we're saying in the long run is that we want to transform the system of public housing from a system where we fund monopoly organizations, public housing authorities, pretty standard top-down bureaucratic relationships, to a system where we empower individuals by giving them the ultimate wherewithal to be able to leave if that monopoly organization, that housing authority, cannot maintain, cannot secure, cannot rehabilitate.

Fundamentally, what we're doing is we're infusing a dimension of market discipline that no amount of bureaucracy can ever do. We can sanction. We can declare. We can threaten. We can issue memos until tomorrow morning.

But the ultimate threat, that they will lose their funding if they cannot keep their residents, like any other business has to do.

Like any other property manager in the country, they have to perform in order to keep their people. They have to make the case, as a business would have to do, is we think the ultimate transformation of the public housing system.

There are a lot of elements of this that we think are important that can happen right away. One of the things we want to do is change the preference rules so that more working families go into public housing immediately.

Just 10 years ago, people who lived in public housing had an average income of about 35 percent of the area median income.

Today, because of Federal preference rules, that is down to 17 percent, the very poorest of the poor. Almost any property manager will tell you that you can't run buildings when only the poorest of the poor are living in the buildings.

We can change that right away by dealing with preference rules.

We can change rent rules as well. I can take you to places where people can tell me that they are worse off working for the take-home pay they receive than if they don't work because of the way our rent rules operate.

I have visited with families who tell me that they cannot stay together, they cannot combine their incomes because it would drive the rent up so fast, that it is advantageous for a family to split up.

The Federal rules have done that, and we can change those immediately.

We can increase the number of residents who are involved, not just in participation, but in management of their buildings.

I'm convinced that's a concept that's very important.

We can require able-bodies residents in public housing to participate in community service, 8 hours a month, nothing onerous, but involvement as citizens with the life of their projects.

We can eliminate some of the more ridiculous rules, such as one-for-one replacement, which today create a circumstance where effectively, we cannot eliminate buildings that common sense tells us need to come down because of pricing.

Because of NIMBYism, because of our own rules, it is impossible to build any other housing in another place and therefore, they cannot bring down buildings and they stand as vacant hulks marring the landscape of city after city across America.

We can substantially improve the workings of public housing. It can't happen easily. It has to happen in stages. We're talking about 1.3 million units in 3400 housing authorities with 4 million people involved.

So when anybody says that this is going to be done from one year to the next with the snap of a finger, it just isn't the case.

We are arguing that we can do this in 3 years for small housing authorities and it may take us 5 or 6 years with the largest housing authorities. But a judicious, temperate, patient strategy of funding development and modernization over the years so that those housing authorities have a reasonable chance to compete when we do go to a certificate or voucher system, is I think the right way to change public housing in America.

We would change the face of cities. We would change the way public housing operates. We would change the whole look of the Federal relationship, the Washington relationship with public housing.

The third and final piece of our reinvention, and I'll be happy, since I see the red light, to deal with most of this in the questions, and I look forward to the questions because, as I said, we welcome a working relationship.

The third piece of our reinvention is the transformation of the Federal Housing Administration from a 60-year-old bureaucracy with 6,000 people, that takes 5 weeks to do an endorsement of insurance, that operates in the culture of a big Government bureaucracy, to a smaller-scale, Government-owned, not privately owned because we must keep the public purpose that operates at lower ranges of the income ladder for home ownership, but that operates as the lean, modern insurance company that it effectively ought to be.

The Federal Housing Administration is important to America. One out of every six new loans for housing in America are FHA loans. First-time home buyers account for 65 percent of FHA's home purchase borrowers and more than 30 percent of all the first-time home buyers in the United States last year were FHA borrowers.

They insured 2½ times as many African–Americans as all of the private mortgage insurers who want to privatize FHA together.

It is a public-purpose organization and it would be a mistake to privatize it. But, clearly, it does have to change. It does have to change because the times require it. We know we can do a better job with new technology. We can go from 6,000 employees to 2,500 employees. We can address some of the pressing problems that, you're correct, Senator D'Amato, Senator Bond is troubled about.

The rate of renewals over the years of Section 8, the preservation of some of the existing stock. And we have some proposals to deal

with that, which I will be happy to deal with in the question period.

In closing, let me speak a few words directly to those who would want to eliminate the Department of Housing and Urban Development. I have great respect for Senator Faircloth and his measure. There are aspects of it that we think are positive.

But the general thrust of elimination clearly would not reform Federal programs or policies, which all of us agree need restructuring.

Those responsibilities would merely be spun off to disparate Federal agencies that have little responsibility or familiarity or understanding of housing issues.

Because there is no way to simply get out of the housing business. Not where we have 4 million people in public housing, an equal number of people in assisted housing, mayors and communities that depend on the Community Development Block Grant programs and the HOME programs and the rest of what we do.

So, there isn't money to be saved in spinning off the pieces. There's only community focus to be lost in spinning off the pieces.

One of the calls that I hear repeated with some intensity is the call to transfer the Office of Fair Housing and Equal Opportunity to the Department of Justice.

This would upset a very careful, constructive, bipartisan agreement that was reached during President Reagan's Administration and the Congress some 7 years ago.

Senator Kennedy and Senator Hatch noted on the Senate floor, the division of responsibility between HUD and the Justice Department to do fair housing in a manner that supported what they could each do best—building on their expertise and keeping separate different facets of the fair housing enforcement—rule-making, conciliation, which HUD does, prosecution of cases on the part of the Justice Department.

This Administration, including Attorney General Reno, supports that negotiated agreement bipartisanly achieved in 1988 and opposes efforts to move fair housing where great damage would be done to this important function.

As much as we would like to say that discrimination no longer exists, the data shows that those patterns of discrimination in banking and mortgage transactions continue to exist and we cannot get the rules level for all Americans without a strong capability in this area.

Let me again just close my remarks by saying that I look forward to your questions. More importantly, I look forward to a working relationship because it is clear the American people want something better and stronger from this agency. I want to produce something better and stronger. The President wants us to do that.

We will only get there by achieving some understandings between the Executive and the Congress and today is the first hearing of this nature since the rollout of our plan.

We look forward to working with you.

I'm told that several other assistant secretaries are here. I'd like to introduce them before I turn over the microphone.

Joe Shuldiner, the Assistant Secretary for Public Housing. That's a relationship with 3,400 housing authorities across the United States.

Marilyn Davis, our Assistant Secretary for Administration, who will oversee this transformation of HUD from an agency with about 12,000 employees to about 7,500, with all of the retirement and early-out and buy-out and all of the difficult personnel issues that implies, downsizing offices from 81 to something substantially less, et cetera.

Andrew Cuomo, is the Assistant Secretary who has within his responsibility the two large funds that we would anticipate creating out of today's Community Development Block Grant and HOME program. Thank you very much. I look forward to working with you.

Senator MACK. Thank you, Mr. Secretary, for your opening remarks.

Let me say that I think that, by and large, all of us support what you have said and are encouraged by what you had to say.

I think the question really that will be developed over a period of weeks and/or coming months is will the Blueprint really carry out and allow to come to fruition those things that you said this morning because I certainly am encouraged by what you had to say.

But—and you and I had an opportunity to spend some time together earlier talking about the Blueprint. My initial reaction was one of guarded optimism.

But, frankly, as I had looked through some of the detail, my concern is that many of us are going to focus on the concept of taking many programs and consolidating them into the three funds.

The real question is the detail of how those funds are then going to be handled. How will decisions be made? What kind of strings will be attached?

Second, I just want to say that I also appreciate the fact that so many from the Department joined you this morning. You're welcomed here and I'm glad that you're with us, and also delighted to have your family with us this morning as well.

Mr. CISNEROS. Thank you, Senator.

Senator MACK. I've got a whole series of questions. I may just skip through some of them to get to some of the highlights and may want to follow up with some written questions to you at a later time.

There's a statement in your discussion of Community Opportunity Fund that gives me some trouble. It says, and I quote:

> Under COF—that's Community Opportunity Fund, HUD will establish national goals while localities will determine how to achieve them.

> This statement redflags concerns that I have about how much real flexibility localities and States are going to have under your performance fund system.

I want to walk through the details of the Community Opportunity Fund.

First, how prescriptive and detailed are these national goals and objectives going to be?

Are they numerical? Are they categorical? Are they going to be prescriptive, more prescriptive than the current requirements

under the CDBG program, which clearly meets the definition of a block grant?

Mr. CISNEROS. Senator, I'm going to be as direct as I may so that we can get through them quickly and all the Senators can have a chance to ask questions and we can stay within your schedule.

First—and respect the mayors who follow me. First, we have in mind programs that are very flexible, that communities can use almost exactly as they use the Community Development Block Grant program today, which does require submission of a plan, and the HOME program today.

We envision two tiers of thresholds that communities should meet.

First of all, no one would want us to turn over Federal money without some safeguards because of the difficulty of graft or corruption that sometimes occurs or misuse of the funds.

The first threshold is, is it being used strictly within the statutory intent, which is to say, accounted for properly, with fiduciary responsibility?

Is it being kept for the low-income targeting the money is intended, as opposed to spread as revenue sharing? And are other statutory requirements being met?

It's strictly what's in the law.

The second threshold——

Senator MACK. Let me just again go back. You're saying that the basic requirements would be not much different than what CDBG requires now.

Mr. CISNEROS. Correct.

Senator MACK. All right.

Mr. CISNEROS. The second threshold is the community plans themselves, where they stipulate from a menu of goals what it is that they want to accomplish—levels of job creation, levels of housing performance, et cetera.

These are not for sanctions, but for entry into the bonus pool of funds that have been set aside.

Those that do a better job of moving their money through the system, spending it on what they said they were, housing production and so forth, those then get to qualify for the bonus money, which is economic development funds.

So what we've tried to do is create incentives to eliminate some of the negatives about the CDBG program and the HOME program, which is it doesn't spend fast enough or it doesn't have enough job creation bang or other specifics of that nature.

The goal is to create positive incentives and those who do a better job at carrying out what they in their own plan say they want to carry out, get a crack at additional funds.

Senator MACK. Under the plan to create a performance bonus fund, you seem to place a premium, as you've just indicated, on the use of funds for job creation and cleaning up urban brownfield.

Mr. CISNEROS. Right.

Senator MACK. Does this create a built-in bias in the program for certain types of activities?

I'm concerned because CDBG has a wide range of allowable uses and a community could be using its funds very wisely and fail to meet certain HUD-established priorities.

Mr. CISNEROS. The priorities will not be HUD-established priorities.

The communities will select from a menu and, for example, if what they said they were going to do is do community clean-up with streets and drainage and low water crossings and so forth, which is the kind of work we did in San Antonio——

Senator MACK. So the bonus is based on their ability to meet their plans.

Mr. CISNEROS. Correct. And then they qualify for a pool of money which does clearly have a more economic development orientation because, Senator, if you'll look at the chart that we've called page 2, most of the money for the bonus pool comes out of programs that are now economically development-oriented.

Frankly, as I look at communities across the country, it is problems related to the loss of economic function and jobs that we need to shore up.

We don't want to do that with the core of the CDBG money because it would mean changing CDBG. We agree with you. We don't want to change it.

But where there is additional money that originally was for economic development, the EDI program, the 108 program, then we think that that money ought to have a tilt toward cleaning up vacant lots and replacing them with economic activity, that kind of thing.

There isn't a city in America, new or old, from Detroit to Tampa, that wouldn't value the opportunity to use additional funding for economic development purposes.

Senator MACK. Senator Bryan, sorry, I did not recognize you when you came in.

Do you have an opening statement that you would like to make?

Senator BRYAN. I do not, Mr. Chairman.

Senator MACK. The Chairman of the Full Committee?

Senator D'AMATO. I'm of necessity going to leave because my colleague and I are on the Finance Committee, and we're holding our second day of hearings on welfare reform.

I might add, Mr. Secretary, I am very much encouraged by your presentation at this point, but I share a concern that Senator Mack touched on. And that's as it relates to the bonus money.

I have a problem if bonus money is specifically set aside for economic development because it seems to me that we ought to give that same menu preference to that community if a community has done a good job in meeting targets and goals and therefore qualifies. Why, restrict bonus money just to economic development, when, indeed, a community may say, well, we need this for senior citizen housing. We need this for a whole other array.

So I would ask you to consider that.

Mr. CISNEROS. Senator, we've been talking—I've been talking just about the Community Opportunity Fund. The affordable housing fund, which is the housing one, has the same bonus. And that is strictly affordable housing development.

So I don't disagree. We can work on that. But the concern that the money for housing would somehow not be available, that's in the other fund.

The CHAIRMAN. Well, again, I would hope that we would give to the local communities the greatest flexibility, obviously within the guidelines prescribed that the dollars be used within certain stated purposes. And particularly as it relates to communities who have done a good job.

I thank the Committee and the Chairman for giving me this opportunity to make these observations.

Senator MACK. Thank you.

Senator Moseley-Braun.

Senator MOSELEY-BRAUN. Thank you very much, Mr. Chairman.

I, too, am a Member of the Finance Committee and so I'll have to go there.

But I have some concerns that I'd like to address to the Secretary regarding the vouchering out proposal. I have some concerns that the elimination of Section 202 for elderly housing, Section 811 for disabled housing, will not be—that the intent, the goals of those initiatives will not be met very well by a vouchering approach. These populations may not be able to avail themselves of the opportunities that vouchers might create.

Mr. CISNEROS. Senator, it was not possible to put together a plan that gets to this level of simplicity without making some very hard judgments. And among the hardest for me was the grouping of the Section 202 program, which is our elderly program and one of our most successful, and the Section 811 program, our disabled program and one of the most successful, into the affordable housing fund.

Let me make clear.

We are not vouchering out housing for the elderly or the disabled in any part of our plan.

First, with respect to the affordable housing plan, this is not vouchering out. This is creation of one of those funds. Localities will be the ones—they'll have more money now because the money is going to the local community and they will have to be the ones to do what we've been doing nationally with Section 202 and Section 811.

That's part of why we stipulated that 30 percent of the money in this fund needed to be used for nonprofits, because it's been nonprofits like B'nai Brith and others, national church housing and others, who have done the bulk of the Section 202 and the Section 811 housing.

They can still do it, but the action will shift to the local community. It will shift from Washington to local housing plan.

Even in our other program, the certificate program for public housing, where elderly public housing buildings exist, we are not requiring the tenant-vouchering of those buildings.

The vouchers will stay with the unit because we want to keep the unit elderly housing and the people will not have to make a move.

So we've tried to be attentive. As for this issue, Section 202 and Section 811, the only thing I can say is that I know that there are members of the Senate, and specifically Senator Bond, who has talked about our reinvention that would not go as far as we have. They would keep the Section 202 program and the Section 811 program separate as existing, separate national programs.

We think there's a cheaper way to provide elderly housing at the community level. But we respect Senator Bond and others of you who may want to keep those programs separate.

That is a decision that you will have to make.

Senator MOSELEY-BRAUN. The second issue that I'd like to raise has to do with the inventory. You kind of touched on it a little bit, the actual physical inventory that's dedicated to elderly housing, primarily what will happen to that once you start vouchering out or providing certificates.

Mr. CISNEROS. Well, that would go to the second point that I made, which is that where there is elderly public housing, not this kind of Section 202 and Section 811, but public housing that is elderly buildings, our plan calls for not ever going to the last step, not ever going to the vouchering for elderly, but the voucher stays with the building.

So the building remains elderly. The unit remains elderly housing and the people never have to go through that process of making a choice to leave. They can know that—because, let's face it. For many elderly people, public housing is not intended to be a transitional step. It is where they go for the rest of their life.

We don't want to frighten them by saying, well, here's a voucher and you make the choice to leave.

They don't want to leave. They came there to be there. And we think that that deserves a separate treatment.

Our plan calls for project-basing, not tenant-basing, the certificates where elderly and disabled are concerned.

Senator MOSELEY-BRAUN. I'm delighted to hear you refer to not frightening people. But I think this is an area that is going to require some clarification.

If anything, the elderly programs have been among the more successful for this agency.

Mr. CISNEROS. No question.

Senator MOSELEY-BRAUN. And now to have the sector that somehow or another, they're going to be forced to move or given a chit or a voucher and told, go for it, that specter is very unsettling to many of our seniors.

I think that it's important that the agency, as we go through this process, make it clear that that's not what's intended to happen.

Mr. CISNEROS. The prospect of certificates or vouchers is frightening enough to everyone—able-bodied residents, mothers with children. It is exceedingly frightening to the elderly and that's why we have changed that part of our plan.

Now, with respect to the others, we believe it is essentially, in the final analysis, the right thing to do because we cannot get performance out of the system in its present form any other way.

But, again, there are Senators, including Senator Bond, whose plan pulls up short, whose vision for what this ought to look like pulls up short of a vouchering system and goes so far as to block grant funds to housing authorities and so forth.

Again, this is decisions that rest with this august body.

Senator MOSELEY-BRAUN. Thank you very much, Mr. Secretary.

Senator Mack. We only have a few minutes remaining in this vote, so we're going to have to go.

We'll recess and we'll be back shortly.

Mr. CISNEROS. That would be fine.

Senator MACK. Thank you for your patience.

[Recess.]

Senator MACK. Senator Kerry, do you want to proceed with your questions?

Senator KERRY. Thank you very much, Mr. Chairman.

Mr. Secretary, thank you for your welcome comments this morning. I would join those who say that I think there are some very exciting, occasionally provocative, but certainly useful, proposals within the context of what HUD has said.

There are some that raise some serious questions, also, and you've heard from people out in the public-at-large.

Let me just ask you if I can a few things.

In your comments, you talk about the need to take a certain amount of time to prepare the public housing stock through the modernization program in order to put it in a position to be able to compete. And obviously, that's very real.

What is the impact—we may be starting behind the curve with respect to that in a way that creates the same sort of self-fulfilling prophecy of lack of capacity to make some of these reforms work by virtue of the rescissions.

I wonder if you would comment on what the impact of the current rescission, the budget cuts, will be on your concept of modernization and management reform.

Mr. CISNEROS. We've been very worried about the rescissions because, as you know, Senator, of the total $17 billion of the House package, $7 billion was from one department. That was HUD.

We carried something like 40 percent of the load for the whole Federal Government. The bulk of that, $2.7 billion, was out of the incremental certificates for 1995. Those waiting lists are now 2 and 3 years long.

That was $2.7 of the $7 billion. Another $1.1 billion was out of public housing modernization, the funds that are available to modernize public housing. $500 million of the rescission was out of public housing development, which is new construction of public housing. Not to mention the hit on operating subsidies and so forth.

So it was a very serious cut.

We've spoken out loud and clearly about that and I've had meetings with Congressman Lewis and Senator Bond and the other appropriators.

Having said that, I do believe yet that the reinvention that we've set out is the best course for the long haul. First of all, it introduces a dimension of market discipline that no amount of Federal bureaucracy can ever do. We can sanction. We can cajole. But we cannot get the public housing authorities to repair, secure, maintain, modernize like the threat of losing residents would do.

Today the residents are powerless. Giving them the certificates, we would give them the power to actually vote with their feet and leave. The housing authorities have to perform.

The trick is not to lose the stock, not to have to make the residents make good on that threat to leave. We want to empower them, but we don't want them to sort of vacate in massive numbers and create hulks of buildings, losing that billions of dollars of stock in the process and moving on to other housing.

The trick is to make sure that the pipeline of modernization funds and development funds continues so that the housing authorities can be in shape to compete.

Senator KERRY. But isn't there a—aren't we creating the impossible myth here in the sense that—that is the trick. It gets even trickier.

Mr. CISNEROS. With rescissions.

Senator KERRY. Correct. I believe there's a $25-billion backlog on modernization. Isn't that correct?

Mr. CISNEROS. I'm not going to defend the rescissions, I cannot.

Senator KERRY. But, no. I'm just trying to test the efficacy of this particular approach.

Mr. CISNEROS. But the rescission was $1.1 billion.

Senator KERRY. In the House, and $835 million in the Senate.

Mr. CISNEROS. The pipeline is about $8 billion deep in modernization.

So, while some is cut, there's a lot there that can be pushed through the system and continue with modernization.

Senator KERRY. OK. That being true, then let me go to the next tier of transitional problem, conceivably. And I don't know. I just want it put to the test.

What happens if 20 percent of the people in a unit decide to vote with their feet and they move? Will that have then undermined the entire viability of that project?

Mr. CISNEROS. No, because what that means is the housing authority can market the remaining—the 20 percent that's vacant. They can market that in the open market and bring families who can pay something of their own income to public housing.

Our hope is that they become more like property managers that are saving buildings by doing the things that property managers have to do to keep them viable.

It puts a lot of pressure on them to keep the building valid so that the 80 percent that's there with the Federal certificate will stay and another 20 percent of people can be attracted there to pay their way and the building begins to take on mixed-income characteristics, which virtually every expert in the field tells me is the absolute precondition to a working building, is to have some measure of income mix.

Senator KERRY. So, I take it, it is your presumption that in answer to those who suggest that a considerable portion, the vast majority of the public housing projects are currently public housing authorities, are efficient and work, and that there's that very small group that are really disasters.

You're in effect saying, there will be a sufficiently high voucher that all of those who are working will continue to be able to work by virtue of market forces that will support them.

Mr. CISNEROS. I'm saying to the good housing authorities, they will be the winners in this system. They really have nothing to worry about.

They will keep their people. The people will use their certificate. They'll use it in the building. The certificate is worth more than the public housing subsidy. They will be property managers. There will be a large number of people with certificates in the building making the financial operations of the building work.

Senator KERRY. Now it's my understanding that, nationwide, about 80 percent of the certificates, the vouchers, work. But in a place like New York City, you come down to about 62 to 65 percent.

Mr. CISNEROS. New York is different in many respects.

On the good side, New York is different in that public housing tends to work. High-rise public housing, which many regard as a failure in other places, works in New York City, principally because, since the Federal Government went to preference rule changes that put a priority on the very poorest, including the homeless going into public housing, New York City, with its very tight market, has less turnover.

New York City, with rent control environment and so forth, has a tremendous pressure on housing and people don't move.

There never was the turnover to replace people at the times that other housing authorities were going under because they were having turnover and replacing people.

New York has maintained to a greater degree than other housing authorities the mixed-income characteristics that we've lost in other places. That's why New York public housing tends to work better than others.

Now, on the negative side, vouchers tend not to work in New York because the affordable housing isn't as available as other places.

New York is different and we have to think differently about how these programs work in New York. There are just a few markets with the same characteristics of New York and that is basically, where there's rent control and other factors to hold the market down.

Senator KERRY. My first round time is up. Mr. Chairman I do have a few more questions. I would just beg the indulgence of the Committee because I have to go down to another Committee for a moment, but then I'll be back.

Thank you.

Senator MACK. Senator Faircloth.

Senator FAIRCLOTH. Thank you, Mr. Chairman.

Mr. Cisneros, of course, knowing the financial pressure that the Government is under, we are $4 trillion, approaching $5 trillion in debt and it's rising rapidly.

The reinvention of HUD will increase spending by $11 billion over the next 5 years. Now I know you say that it saves money, the reinvention. But are all the savings on paper?

My question is, why should we reinvent it and yet, we're going to spend $11 billion?

Mr. CISNEROS. Senator, first of all, there are some disagreements on how much savings there are and it has to do with whether or not we use sort of traditional budget practices of operating off of a baseline or other approaches to calculating how much the saving is.

We contend that we're going to save $13 billion in outlays, $51 billion in budget authority, through the budget practices that have been used over the years.

I will tell you that I share some of the concerns that principally Senator Bond has articulated about the rate of escalation of Section 8 renewals, particularly, because with the new incrementals every

year, 15-year certificates on buildings, 5-year certificates in the mix and so forth, the numbers grow very dramatically and we're going to have to cooperate and come up with some solutions to mitigate the rapid increase in those costs in the out-years.

We're on board to try to help. And we'll offer up some suggestions in the appropriations process.

To go to your question, why should we reinvent if it's not about saving money?

Let me say, I never envisioned that we were starting out on a reinvention strategy because our priority was to save money.

I know the pressures on money and we're attempting to do our part. The truth of the matter is that this is a department that spends only 3 percent of its money on salaries and expenses.

Ninety-seven percent of the money that HUD spends is in communities. You and I both know the need that's out there in the country.

I would like as much as possible to move as much of that money through to communities and hold the levels as much as possible because they're that badly needed.

We've got 4 million people in America who need affordable housing. They're paying more than what they ought to be spending for ramshackle housing.

I think we ought to reinvent this Department because we want to do a better job and not waste money in public housing because we need to do a better job in creating home ownership and because we want to serve communities better. And we ought to save money in the process.

But I'm not driving this reinvention because the intent is to end programs, shrink the effectiveness, and cut the money. I'm driving this reinvention because I want to do a better job in touching people's lives out in the country, and if we can save money in the process, we ought to do absolutely everything we can to do it.

Senator FAIRCLOTH. Well, in looking at HUD's performance over the last 30 years, do you honestly think American cities are better off than they were back in 1965, the year HUD was created?

If you do think so, tell me on what basis are they better off?

Mr. CISNEROS. Senator, I appreciate your question. It's an intriguing question and I noted it when you spoke to this earlier.

First of all, when the Department was created in 1965, the cities were burning.

Senator FAIRCLOTH. I'm sorry? The cities were what?

Mr. CISNEROS. Were burning.

Senator FAIRCLOTH. Burning.

Mr. CISNEROS. It was in part created because of the riots of the 1960's, the urban crisis that was front page for the news magazines, Time and Newsweek of that era.

Forgive me if this sounds like a philosophical retort, but I don't know what kind of shape the cities would be in today if there had been no investment in community development and housing.

I mean, one can imagine in America where we went downhill from 1965. There's a lot of people who would argue that we've slid downhill, but I don't know where we were going.

The cities were burning. There was rioting in the streets. We haven't had regular repeats of those episodes. We've had some peri-

odically, like in 1992 in Los Angeles. But by and large, we kept the lid on as a society and made some progress.

23 million homebuyers, because FHA has existed, 23 million people own homes today because FHA has existed. And last year was the second-best year in FHA's history. 450,000 Americans became first-time homebuyers last year because FHA was in business.

Community mayors will tell you to what uses they have put the Community Development Block Grant program. Public housing—yes, it is a symbol of how we have failed. But there are 3,400 housing authorities and 105 of them are graded as troubled. That leaves 3,300 that are housing people day in and day out and nobody really ever notices them. And some of them, you can't tell the difference between an apartment building and the public housing.

So, yes, we have a whole lot of things to be ashamed about at the Department. But I've got to believe that America is better because somebody's been paying attention to housing and community strategies over the last 30 years. I sincerely believe that. I also sincerely believe we must do a much better job.

I sincerely believe that if we can pass this reinvention, you would be proud of what you have helped create over the next decade as community policies work even better.

Senator FAIRCLOTH. One quick question, Mr. Chairman.

Of course, as we all know, the Senate has been debating rescissions that will cut HUD spending for this year. The newspapers, which I don't always believe, indicate that HUD is spending money rapidly in order to spend it before it can be cut. Is this true, and can you give me assurance HUD is not doing that?

Mr. CISNEROS. I can give you assurances, Senator, that we are not spending at an extraordinary rate. That is to say, we have made no special efforts to push money out the door because we envision the rescissions coming. I'll give you an example.

One of the rescission items in the House package was$550 million for the program called Hope 6, which gives large sums of money to housing authorities to renovate complete developments.

A winner in the first year, as you know, was Charlotte. In the second year there were eight others.

The Senate, in its appropriations report last fall, gave us explicit direction to move that money out, to go right to the previous competition list and fund the cities that had been granted planning grants in the last cycle.

We did it in January. That appeared on the rescission list in February. Someone could say that we were accelerating that money.

It is not true. We were meeting the instructions that we had to go through that competition process, or through the competition list.

No, I can assure you, we are not. We are being very careful and the General Counsel of the Department is here and we meet. He has instructed me on what constituted obligation and what doesn't constitute obligation and what constitutes any extraordinary measures versus what is in the normal course of calendar.

We're sort of caught between a rock and a hard place. There's a law that tells us that we cannot artificially impound money and hold up waiting for possible congressional action. And on the other

hand, there's good sense that tells us that we ought not try to circumvent Congress by moving the money faster than normal years.

We are not moving it faster than can stand scrutiny.

Senator FAIRCLOTH. I thank you.

Senator MACK. Senator Bryan.

OPENING COMMENTS OF SENATOR BRYAN

Senator BRYAN. Thank you very much, Mr. Chairman.

Mr. Secretary, let me first of all commend you for a very forceful presentation and I think a very imaginative reorganization plan here that you've submitted for our consideration.

I'd like to follow on first on a point that you made.

Not everything that HUD has done, has been wrong. Of the four public housing authorities in Nevada, three are quite good.

I had occasion not too long ago to visit one of those housing authorities, not high-density, not high-rise, in which the properties were better maintained than private- sector properties right across the street.

That belies the image that unfortunately some of your failures have projected to the media.

My question deals with FHA. I think it is a very important program. You used one out of six, I believe, in your opening testimony. In some parts of the country, for us in southern Nevada, it's even higher than that.

I'd like to know specifically what your reorganization of FHA contemplates. I'm not troubled by the creation of this Government corporation. What I would be interested in knowing is what groups or categories of individuals under the current law that are eligible for FHA might no longer be eligible under your reorganized concept?

Mr. CISNEROS. Senator, the reorganization changes really nothing about the eligibility or focus of FHA. What it goes is change the organization in order to be able to accomplish the mission more expeditiously.

Frankly, what we have is a 6,000-person bureaucracy using old technology with 81 offices across the country. It takes 5 weeks to do the endorsement of the insurance. That operates out of a Government culture instead of the insurance company culture that it ought to.

What we're trying to do is to get around some procurement rules so we can get technology, get around some traditional civil service rules so that we can get the kind of financial and insurance expertise that a company ought to have.

Senator BRYAN. I am for that, Mr. Secretary. I want to be clear. And I note that in the letter that we have addressed to our Chairman, that there's a broad coalition of private-sector organizations that deal in housing from the American Institute of Architects to the homebuilders and others.

But let me again reframe the question. I agree with those objectives. FHA is a troubled bureaucracy and all the delays that you've mentioned have been a major concern for us.

But let me just make sure that I have a direct answer.

Are you saying that if we approve the reorganization as you have submitted it, with respect to FHA, that there is no change with re-

spect to those individuals who could qualify and be eligible to participate in FHA?

Mr. CISNEROS. Yes, Senator, that's what I'm saying. And let me just expand, if I may. I want to make reference—I said earlier that there were elements of Senator Faircloth's bill that I applaud. One of them was the Senator's recognition of the need to create a new structure for FHA and keep it as a public purpose organization.

There are those who would want to sell off FHA to the private mortgage insurance company. But we lose the public purpose that has made it possible for people at the lower ends of the income ladder to become homebuyers, and that is very important.

We believe we have a unique opportunity in the country, Senator which we would like to make a bipartisan effort. We believe there's an opportunity in America between now and the end of the century because of the way forces are converging to have an all-time high home ownership rate in America achieved by the year 2000.

The previous high was 65.5 percent in 1980, and we've dropped off since then. But the convergence of a good economic picture between now and the end of the century, five years, immigrant populations that have been saving money and are ready to buy, minority populations which, if we could just deal with some of the discrimination in the marketplace and get them up from their 45-percent home ownership rate, which is 20 percent below the national average, we can get that 64 percent which we are at right now to something around 66 or 67 and we would be higher in terms of the percentage of Americans that have ever owned their homes.

That's why we need a public purpose FHA, a leaner FHA. And that, I think, would be a wonderful celebration at the end of the century of what it means for America to be at peace, out of war, and prosperous for the greatest number of Americans in the history of the country to own their homes.

That would be something worth celebrating and we would have accomplished that together.

Senator BRYAN. Well, I agree with that objective and I obviously am a very strong supporter of FHA.

Let me just say that with respect to taming the bureaucracy, that is a humongous problem. FHA and HUD generally have bureaucratic problems that are of staggering impact.

Mr. Secretary, I had a meeting with our southern Nevada office fairly recently, in which the various functional categories—that is, single-family, multifamily, and you will know the other various categories—that nobody in that office has the ability to give you a decision. That is, rather than having somebody traditionally in charge of that office, where if you have a difficulty, you disagree with the decision at the public housing or the multifamily or the single-family have.

Today, what we are told is if you disagree with the decision of single-family, then you've got to take that decision to San Francisco or you've got to take it to Phoenix.

I have to tell you, in terms of improving the problems with the bureaucracy, that has had a horrendous impact.

In other words, you can't call an office, whether you're a private citizen or a Member of Congress, and say, I'd like to speak to the person in charge. We have a problem in this aspect.

They will tell you, I'm no longer in charge. All I do is provide the pencils, the paperclips, the xerox machine, and if you have a difficulty with the decision that one of my people have made in single-family or multifamily, you have to then go to their—whatever you call it, a regional office.

Could you very briefly respond? And I apologize for going over my time.

Mr. CISNEROS. Yes, Mr. Chairman. Let me just briefly respond by saying——

Senator BRYAN. Because I must say that it is extraordinarily frustrating.

Mr. CISNEROS. I recognize the problem you describe.

As you know, I visited at your request the Las Vegas office.

Senator BRYAN. Yes, you have and I appreciate that.

Mr. CISNEROS. And I saw there a situation where the bureaucracy was so bad that when I arrived at the office, unannounced, there was no receptionist, but a telephone with a sign that said, pick up the phone and you can talk to someone in the office.

Senator MACK. I would imagine they were fairly surprised at that.

Mr. CISNEROS. Yes.

[Laughter.]

Senator BRYAN. That's the Government concept of user-friendly, Mr. Chairman, yes.

You're quite right, Mr. Secretary.

Mr. CISNEROS. Nic Retsinas has delegated more and more authority at a lower level of FHA and he describes to me a tremendous taking up of that authority at the local offices.

But the problems you describe are the reasons why we have to change from the Government structure or something more like a company with clear goals and missions, so that they can function entrepreneurially.

We will go from 81 offices to substantially fewer and three processing centers across the country that have the computer capability to do what a modern insurance company does today in providing insurance.

We hope to sort of change the culture from a Government culture to a service culture, and that's the kind of thing we want to address, the problem you raised.

Senator BRYAN. If the Chairman will indulge me a moment, just an anecdotal point.

As part of that tour, Mr. Chairman, I asked somebody who was not working on a piece of equipment why they were not working on a particular computer. They said, "well, it doesn't work." I said, "well, how long?" The person said, "it wasn't working when I went on vacation." I said, "when was that? Three months ago."

That is the kind of bureaucracy that you have that just frustrates everybody.

Mr. Chairman, thank you very much for permitting me to overstay my time.

Senator MACK. Thank you. Mr. Secretary, as you can imagine, there's a whole series of questions. I think that it's now almost 11:45 a.m. and we have three mayors that are waiting.

I very much appreciate your testimony this morning. One of the areas that we didn't get a chance really to get into is the Inspector General, HUD's Inspector General basically testified before the Committee that more effort, not less, is going to be required during the implementation of the Blueprint.

Mr. CISNEROS. Right.

Senator MACK. I'm going to forward some questions to you with respect to that area.

Mr. CISNEROS. Sure.

Senator MACK. That is of concern to us. Again, I thank you for your testimony this morning.

Mr. CISNEROS. Senator, let me just say, I'm dedicating all of my time and the highest priority to this effort, to redesign of HUD, curtailing travel, speaking appearances, and all the rest, to work on this.

If I can be available to you one-on-one, Senator Faircloth, to answer questions, we look on this as a working relationship. You send me questions in writing or you pose them to me personally, I will personally be there to work with you.

Senator MACK. I appreciate that and I look forward to working with you.

Mr. CISNEROS. Thank you.

Senator FAIRCLOTH. Thank you.

Mr. CISNEROS. Thank you.

Senator MACK. I want to thank the three mayors for joining us this morning, and apologize for the time.

I have not had the pleasure of being with Mayor Goldsmith, but we're delighted that you're here.

Mayor Schundler, it's a delight to have you with us. I've visited your city and we've had an opportunity to talk in the past.

Mayor Dennis Archer, I'm delighted to have you with us. It was great to see you in the State of Florida not too many months ago, and I look forward to continuing our dialogue and at this point, look forward to your testimony.

Mayor Goldsmith, I know you have, I think, some time constraints, so why don't you go ahead and then we'll listen to the other panelists.

STATEMENT OF STEPHEN GOLDSMITH, MAYOR, INDIANAPOLIS, IN

Mayor GOLDSMITH. Thank you very much. I'll keep my remarks brief and stay with you in the attempt to answer questions.

Let me speak at a general level first.

I think that the strategy of cities over the last couple of decades has been self-destructive. Mayors from large cities, and we're the 12th largest city in the country, have advertised our cities as such awful places that you should dump enormous amounts of Federal money in to save us from ourselves.

I think this pity strategy really needs to change.

At least I'm here to say that our cities are great places. They have problems, but the Federal Government many times aggravates those problems rather than produces a solution.

We have an opportunity here, I think, to change that.

What we need in urban corps are not programs. We need wealth and we need people. We can address how together to create those, understanding that the primary way to create wealth is not through Government, whether it's your Government or my Government. It's through the marketplace.

To the extent that we can use the marketplace to create opportunity is the best way to produce an organized success in cities.

I am delighted to have the opportunity to comment on the Secretary's presentation. Before I do that, I don't want to fall into a trap here because I fundamentally believe that what we don't need are more programs.

Tax policy is a much more efficient way, for example, to create investment than Federal grant programs. They're more efficient. We don't need any bureaucrats to administer them. They provide tourniquets to the flight of wealth. They reduce absurd program requirements because they don't exist. They leverage private dollars. They take the grantsmanship system and make it more rational.

I'm delighted to comment on the Secretary's proposal.

For my part, I'd rather just have none of those programs and tax incentives as a way to create affordable housing and a better standard of living in my community.

With respect to the reforms for HUD, I think the Secretary's proposal and the principles are excellent. And in terms of where HUD is today, they're a dramatic step in the right direction.

My only comment is I'd like to take that dramatic step more forcefully and more quickly, and let me make a couple of observations about that.

The problem with HUD today is that it spends money because of all of these bureaucratic restrictions and some congressional restrictions, in a fairly absurd way and creates wasted money and lack of opportunity.

Without going through all of those because there's literally hundreds—any time you try to do top-down planning for several million people, it's not going to work and there are hundreds of examples.

But in my public housing, it will remain bad until a number of things change, one of which is the one-for-one replacement rule that HUD forces on us, essentially telling us if we can renovate housing and take efficiencies and make them into one-bedrooms, then we have to create some more public housing somewhere else which operates at a deficit, so we aggravate the deficit and continue the problem, et cetera.

These problems—the HOME dollars, which many of us are happy to spend. I recently said to my director of this program, I want to go out and I want to renovate as many owner-occupied houses as possible so that people won't have to vacate their houses in our tough neighborhoods.

They responded, you can't do that with HOME dollars because we have to fully bring every dwelling up to code requirements if you do that. And the code requirements are so high that we can't afford to fix them up.

Those hundred homes are still sitting out there until we raise local dollars to do them because it would have required a waste of money.

CDBG funds, which are the most flexible of funds, even though they have their own sets of restrictions. We pass all of our CDBG money through to our community groups.

Many of us have in these troubled neighborhoods, these old facades, these old retail intersections where people have left because of poverty or crime or mega-centers. And I said I wanted to fix those up. I was going to offer CDBG dollars to neighborhood groups to fix up the retail corners.

I'll exaggerate. The Federal police force knocked on my door and said, you can't do that. And I said, why? Because, they said, if you pay a minimum wage to unemployed youths in the neighborhood to fix up the facades with CDBG dollars, you violate Davis–Bacon and therefore, you can't use the money for this purpose.

So the facade is still there and it's still messed up. Neighborhood kids are still unemployed and the CDBG dollars are invested elsewhere.

HUD in my community is a slumlord, despite the best intentions from HUD. The highest executives in HUD have been very creative in problem-solving.

We have a place called Hometown. I call it Cracktown. It's dilapidated, awful housing. It shouldn't have been built in the first place. It's a home for crack dealers. It ought to be torn down.

We had every top official in HUD trying to help us figure out how to get around Congressional restrictions so that we could tear it down. It took 2 years, with the commitment of the Secretary himself, to do that.

Having said that, just a couple of one-minute observations on the plan.

First, let me slow down for a second because I think we're in a very difficult time here.

HUD wastes a lot of money. The Government wastes a lot of money.

Slashing money in existing programs is probably the worst of all worlds because it leaves the micromanagement, the overregulation from the top down, forcing us to spend money in absurd ways and then cuts the programs.

All it does is accelerate the deterioration of affordable and public housing.

What we need is a dramatic rethinking of the whole process, part of which is in the Secretary's document. I would rather you tomorrow gave me a deed for all of my public housing, tomorrow, and vouchers for the people that live there, and if they don't like the way I take care of public housing, let them move, so long as we have an opportunity to get started in a rational way.

I have a responsibility to produce housing.

My request simply would be that we radically change the programs. And if we use the vouchers, market-based systems to do that, you can save money, I can save money, and we can increase the quality of affordable housing.

I think vouchers, tax credits, block grants eliminating one-for-one conversion, are all strong ways to do that.

Finally, when I read the document, the reinventing document, some of us mayors are a little frustrated that the cities aren't rec-

ognized by the Federal Government any more. Only States. Which is a movement in the right direction, but we're still here, too.

As you think in creative ways, the more we connect these opportunities to real people, poor folks in my community, or to the cities themselves, rather than just transferring a Federal program to a State program in its existing format, I think we could produce a lot more value for our citizens.

I would urge you, Mr. Chairman, and Members of the Committee, that this Blueprint, in my opinion, is a dramatic step in the right direction. I would just do it more quickly and more forcefully, vouchering out as much as possible to give citizens, poor folks, real control over the decisions in their lives.

I think that will benefit all of us. Thank you very much.

Senator MACK. Thank you.

Mayor Schundler.

STATEMENT OF BRET SCHUNDLER, MAYOR, JERSEY CITY, NJ

Mayor SCHUNDLER. I want to thank you for allowing me to testify today.

I also want to acknowledge, as has Mayor Goldsmith, that Secretary Cisneros's steps are in the right direction.

I also want to encourage you to be more bold in your thinking about overhauling our social welfare programs.

Most of the testimony that you've been hearing deals discretely with the issue of housing as if that need exists in a vacuum.

Much of the discussion specifically is on how HUD could provide housing for the poor more efficiently.

But I want to suggest that a more enlightened approach to social welfare programs would take a broader view of the whole person.

For instance, I suspect that you not only feel good about the fact that you can choose where you want to live, but also about the fact that you earn the money with which you pay your rent or your mortgage.

Now having Government voucherize housing assistance is better than having Government ghettoize the poor in housing projects.

But more fully reforming our welfare and tax policies so that every American can feel the satisfaction of actually earning the money with which they pay for their housing would go a long way towards making Americans whole, just as you are whole in taking care of your housing, and make them have that same feeling of satisfaction.

Now to this end, before I actually comment on the specifics of the reinventing document that the Secretary has put together, I would like to focus on a simple proposal, and that is that we would combine a move away from welfare towards workfare with Congressman Armey's Flat Tax Proposal and a set of non-means-tested, refundable earned income tax credits that would be earmarked for housing, food, health care and day care, all of those, let's say, in one block, if you will, a tax credit that could be used for any one of those things, except perhaps for the health care credit, which would be specifically received when someone buys insurance.

They either buy insurance for themselves or they give the money to the Government so that we can make sure that they do buy insurance for themselves.

Now under this proposal, all Federal welfare programs of providing cash assistance for employable adults would be replaced with federally financed but locally administered workfare programs. These workfare jobs would not have to be publicly administered. They would not have to be, in short, Government make-work jobs.

They could be federally funded jobs with private- sector firms which are competitively contracted at the local level to provide various supplementary public services.

For instance, I have neighborhoods where the needs are very great for everything from day care to cleaning up the street to, let's say, augmenting our police force with, as we could, private security guards.

We have enormous numbers of people who are unemployed. Why pay people not to work when instead, we could actually give them a paycheck and allow them to upgrade the quality of our most distressed neighborhoods, working for a firm which has to produce or it can be fired, and then another management company would come in and utilize that labor more effectively to upgrade the quality of life in that neighborhood.

Now combining a flat tax rate with refundable earned income tax credits would, even without means testing, produce significantly progressive, effective tax rates.

Making these tax credits refundable, in the sense that if you can't use the full credit because you don't have enough income, you would actually get money back, as is the case with the earned income tax credit that we have today, would ensure that all Americans would equally benefit by this system, including very low-income working people who cannot use a simple tax credit fully.

Attaching these tax credits to earned income would specifically increase the rewards for work. I personally don't believe that Government should be subsidizing those who refuse to work or those who do not need to work.

Making these tax credits non-means-tested would correct the perverse incentives of the current tax code, which reward Americans for staying poor and which harshly penalize them if they work hard to climb out of poverty, or if they form a family and thereby increase household income.

Now, right now, today, in Jersey City, the average AFDC family is a woman with two children who earns a total package worth $20,000 a year. If you take a private-sector job, you'll make $12,000 and you'll lose your benefits, but you'll be taxed.

In this system, it depends on what your income is. But if you have a workfare job and you get a paycheck, it's no different than if you have a low-paying private sector job. You'd still get the benefits.

As you make more money, again, the earned income tax credit decreases and ultimately, you become a net payer instead of a net receiver of the benefit.

But this is something which always makes it so that every dollar extra that you earn, you at least keep, let's say, 80 percent of it.

So you are rewarded for working harder, instead of having someone who takes a private-sector job be penalized for taking that private-sector job.

Now targeting these tax credits to the essentials of food, housing, health care and day care would satisfy the Government's interest in making these essentials more affordable, while at the same time allowing for the elimination of other tax and income benefits.

For example, deductions for mortgage interest and employer health care contributions could be eliminated, as could other federally administered food, housing, health care, and day care assistance programs.

People would be able to buy their own health care with their own money instead of giving it to the Government.

Now these welfare and tax code changes would require less bureaucracy and would cost less to administer than our current social welfare programs and would also ensure that no one would have an incentive to stay in a workfare job if they could find a better paying private sector job.

Finally, for the first time, every American who was willing to work would be able to obtain a job, whether private sector or workfare related, and that, together with the earned income tax credits, would net them up to a livable wage where, they could choose to live where they want to, and they could pay for that rent with money they have earned, which is a totally different approach than the Government entitlement system that we've erected.

This is really the plan that I and several other mayors from around the country would like to recommend to you as a way to fully overhaul the Federal Government's approach to providing social welfare programs.

But to focus more narrowly on the Secretary's recommendations, HUD currently has three major missions.

Its first mission involves the distribution of urban development grant monies.

Just to bring my remarks to a close, I'd like to see that brought into one block grant, maximum flexibility being allowed to the cities.

My personal preference, as Steve has said, you'd actually block grant it to the cities, not to the States, based on a formula which would take politics out of it. It would not penalize us if we actually began to do financially better locally, but it would give us those resources to use in a way that has the maximum positive impact on our communities.

The second major mission of HUD as it is currently operated is to facilitate the construction and management of public housing projects.

I don't think I have to go into the fact that almost all of us at the local level are not keen on that approach. The Secretary's recommendation that we move towards vouchers would be a significant improvement.

The only thing I would suggest, they are obviously talking about a fairly significant amount of capital investment during this transition period.

I would argue that as a quid pro quo for that capital investment, there should be a requirement that the end of that transition period, that housing be turned over to local hands.

Again, that the rules be clear that the housing authority has the right to even sell it to, for instance, a not-for-profit charitable orga-

nization which might run that housing. And not that we have to have this housing which continues to be Government-controlled.

My sense is that if you do that, you'll be ultimately continually putting new investment monies into that and that will steal from the dollars that you have available to provide voucher assistance.

Finally, the third mission of HUD is mortgage finance, principally through the Federal Housing Administration.

If the FHA is to assist in the Federal Government's efforts to revitalize our cities, it should refocus its efforts on providing home ownership opportunities at the very low-income end of the mortgage market.

As you know, this has not been the way that HUD has been operating. Change is long past due to target those monies towards those who are at the low end of the income scale.

In closing, I would just add this final thought.

I believe that you have a historic opportunity to redo America's social welfare programs, as opposed to looking at housing discretely and as opposed to, let's say, cobbling a few reforms within the Department of Housing and Urban Development.

I would request that we take a more encompassing view of our total approach to providing for the social welfare of the American people.

If we follow the route I'm proposing, obviously we'd be able to very significantly decrease the federal workforce and payroll.

But more dramatically, you would give people the opportunity to know that they could find a job and make enough money even at the lowest wage jobs to take care of their families. That would be putting them back on the road to being full persons who can truly feel that this is a country of opportunity and a country that guarantees that they'll be able to take care of the essential needs of life.

That's something that all of us feel good about in our own lives, and I think it's something that we should want for the least amongst us.

Thank you very much.

Senator MACK. Thank you, Mayor.

Mayor Archer.

STATEMENT OF DENNIS W. ARCHER, MAYOR, DETROIT, MI

Mayor ARCHER. Good morning. I think.

Senator MACK. You just made it.

Mayor ARCHER. Perhaps good afternoon.

[Laughter.]

I'd like to thank you both for the opportunity to be present and to present testimony to you this afternoon.

On January 1, 1994, when I became mayor of Detroit, I was confronted with the following grim demographics.

A population of 1,027,000, of which 32.2 percent, according to the 1990 census, or 328,000 of us, were living below poverty. 46.6 percent of our children live below poverty.

Over 115,000 Detroiters are without any jobs. 35 percent of our people cannot afford to buy or own a car. And approximately 6000 men, women and children in Detroit are homeless.

Our city is 76 percent African-American, 2 percent Hispanic, 1 to 2 percent Arab, Caldine and Asian.

In other words, our city is 80 percent ethnic minority majority.

As an aside, Michigan's second largest city is Grand Rapids, on the western side of the State, with a population of 200,000. Indeed, we have more people in Detroit who live below poverty than all the people who live in the entire city of Grand Rapids.

In fact, the number of poor people in Detroit are equal to about half of the entire metropolitan area of Grand Rapids, which purports to be able 700,000 people.

But we've been working hard to overcome these problems. And HUD, frankly, has been a very strong partner. Detroit put together the best empowerment zone application in the United States. We worked from the grassroots community up.

Through our business and governmental leadership, we developed a public/private partnership that resulted in a financial commitment in large measure encouraged, I believe, by the Community Reinvestment Act, of $1.974 billion for a 10-year investment period.

In addition, Detroit renaissance, which is made up of 42 of the largest corporations in southeastern Michigan, the automotive Big Three and others, will raise up to $60 million for access to capital.

MBD Bank, which is the largest holding bank in the State of Michigan, along with Quest Realty, will raise up to $50 million with a special emphasis on access to capital for minority businesses.

Our foundation community has committed $10.5 million for a fund to revitalize housing and commercial developments in our neighborhoods.

Our two Detroit pension plans are reviewing a proposal made by me to invest $60 million, most of which will be to build affordable housing. And the national AFL–CIO, through their pension plan, is looking to consider investing $50 million in the city of Detroit as it relates to housing as well.

Nonetheless, Mr. Chairman, for Detroit to succeed in its mission to once again become a world-class city, it is important that we talk about consolidating HUD programs and not cutting the Department's funding.

By cutting public housing development, public housing modernization, incremental rental assistance, and other important HUD programs, the recent rescissions will cause serious harm to Detroit. Cities will still have overwhelming needs.

Whatever shape the debate takes place here in Washington will not alter the fact that housing and community development needs of citizens across this Nation will still have to be addressed.

As mayors, we know that there's still a great deal to be done. The U.S. Conference of Mayors' most recent status report on hunger and homelessness in America's cities, a 30-city survey, makes the extent of the need very clear.

The report found last year's applicants for assisted housing waited an average of 21 months for public housing, an average of 36 months for Section 8 housing, and an average of 35 months for vouchers.

Sixty-three percent of the cities have stopped accepting applications for assisted housing programs due to excessive length of the waiting list.

With conditions such as these, I urge both Subcommittees to support at the very least the fiscal year 1995 funding levels for HUD's public housing programs.

HUD was started, as was mentioned by the Secretary, during an era of social change that also included the Civil Rights Act and the Voting Rights Act. The creation of HUD was the recognition of the fundamental importance of providing minimal standards of shelters for citizens.

Since its creation, HUD has made homeowners out of many citizens who otherwise would not know the stability, security and the pride of saying, this is my home, which goes to, I think, Senator Faircloth, your question earlier.

If we eliminate HUD, where will these people live? Most cities like Detroit have been suffering from an ever-decreasing tax base. Since 1950, Detroit experienced a population loss of nearly 800,000 people.

In the 4 years from 1988 to 1992, the Detroit metropolitan statistical area lost 39,206 manufacturing jobs and 8398 construction jobs. The impact of this job and population loss on the tax base and the economy of Detroit has been devastating.

Detroit has been left with the disproportionate number of poor and limited income people. Will the suburbs absorb them? Will they live in rural areas?

Detroit's public housing system, although improving, is a troubled one, one that I inherited. Public housing is still home, however, to 4570 families, of which 1715 are senior families.

If we do not house them, who will?

I agree with many of you on one central point—we do not need the 1980's version of HUD rife with, as we later learned, corruption and scandal.

I'm of a new generation of mayors in the United States.

My generation will not stand for the slightest hint of corruption or public disservice.

Secretary Cisneros has taken the initiative to restructure and reinvent HUD. This reinvention, which you now have before you, will make HUD more efficient in delivering services to our Nation's citizens.

The reinvention of HUD will call for new accountability. HUD will ask simple questions of its programs.

How many people are homeowners now who were not homeowners before?

How do we lower the delinquency rate on the payment of rent owed to HUD?

How have we provided more low-cost housing to citizens?

Programs must be able to stand on their own merit. Also, communities must be rewarded for high levels of achievement.

Why not a bonus program? If we do everything that we're supposed to do, and do it in cost savings, why not have that bonus opportunity available to us in each of the categories?

The reinvention of HUD means the city of Detroit will have to consider three performance-based funds instead of 60. We will not have to spend unnecessary time applying for multiple grants, filling out paperwork, attempting to plan around several sources of Federal funds.

Detroit will be able to concentrate on solving the problems of housing.

The reinvention of HUD means that nonprofit, community-based organizations will help determine what is in the best interest for the citizens of our cities, not a Federal bureaucracy in Washington, DC.

The reinvention of HUD means that more people will be able to afford their own homes through its Government-owned insurance company, combined with public and private sector partners.

HUD will simplify the process for many of our working poor to buy a home. The reinvention of HUD is also a reinvention of an attitude of an agency, something that Senator Bryan talked about before he left.

HUD will become user-friendly and address the most important need of our Nation—the housing needs of our citizens.

The poor and low-income citizens of Detroit and of our Nation who need public housing suffered through years of inefficiency in HUD during the 1980's. We don't need that again.

Most people want to own a home. The number of homeless people is increasing. The current rescissions will make what was intended to be a housing safety net a worthless relic.

Simply put, these rescissions that have been proposed will decimate housing for citizens in Detroit and most of our Nation's cities. Thousands of hard-working, wage- earning taxpayers who cannot afford housing without Government assistance will not have a place to live.

In Detroit, for example, we want to start the demolition of unsafe, abandoned property so that Detroit can make these sites economically viable.

In Detroit, we want to start creative and innovative home ownership programs to transform our public housing, parkside homes.

I cannot and I must believe that our Nation's mayors cannot make life better for our citizens if we're going to be shackled by these rescissions.

The feasibility of the private sector, of Detroit being able to create over 1000 units of affordable housing, decent housing, is pure folly.

For many of our Nation's poor, low-income, and disabled people, the only housing option is HUD.

As legislators, as prudent public service in this area of scarce economic resources, the most viable option in my humble opinion is an efficient HUD. An elected official who every day sees the impact of outdated, inefficient public housing policy, my own opinion, my only option right now is HUD.

HUD represents a real investment in our cities and in our citizens.

In the current fiscal year, HUD is providing $24 million in operating grants, $32 million in comprehensive grants to help provide public housing in Detroit. In addition, HUD has awarded $187 million in special grants this year to assist Detroit in bringing the quality of public housing in Detroit up to basic standards.

Elimination of this needed agency would send the message to our country that you just don't care, and I don't believe that on the

basis of what I'm hearing and the questions that have been going forth.

I'm here today on behalf of the homeless, the poor, the low-income people for whom HUD has and can make a difference.

Also, I'm here today on behalf of all those mayors who believe as I do, who see and live with the pain of the growing poor and the disenfranchised, homeless population.

Finally, I'm here as a person who is deeply concerned with the growing insensitivity towards the poor.

Thank you.

Senator MACK. Thank you, Mayor.

Again, I want to express my appreciation for all three of you. You are great advocates of the people of your cities and I would broaden that—you're great advocates of the people of our country.

Again, I appreciate your comments today.

Senator FAIRCLOTH. Mr. Chairman.

Senator MACK. Yes.

Senator FAIRCLOTH. I'd just like to say that I really appreciate your being here and taking the time.

I am going to have to leave, but I thank you and I realize the sacrifice and the time to come, and I appreciate what you had to say.

Mayor ARCHER. Thank you.

Senator MACK. I then will speak for my colleagues.

[Laughter.]

Raise a series of questions. And I think the first couple of questions that I raise will be open for each of you to respond as you will to the question.

One of the major HUD reforms we are considering is consolidating programs and sending the funds in the form of block grants to the States and local communities.

We are concerned, however, about the capacity and staff resources at the local level to carry out these programs.

Could you comment on this concern and tell us how you city intends to manage these resources?

Mayor GOLDSMITH. Senator, I appreciate the question and I think it contains the answer as well.

We're a great basketball State.

Senator MACK. I've heard that.

Mayor GOLDSMITH. Thank you.

[Laughter.]

Generally the official closest to the action makes the best call. And the idea that a Federal official tells a state official tells the local official tells the neighborhood person how to tell the poor person how to live and that produces value somehow is perverse.

My answer to you, Mr. Chairman, is that I'm all for devolution. But that is only a half-step.

The way that we would respond would be to open up many of these services to the private sector to purchase the capacity to cause neighborhood-based groups, private developers, not-for-profits, all to participate.

Most importantly, and here, maybe my views differ a little bit from my colleagues.

Poor folks deserve a decent place to live. If they have a voucher to spend, I'm confident that our market place will respond and produce that housing, much more efficiently than the system now.

The more the funds are—proposed two, actually three large block grant programs. I'd have one block grant program.

If you would cash out all the money you're spending in my city, take about 10 percent back for your own good, give me 90 percent of the money and say, here, you're in charge of poor folks and housing in your community, here's your check, we can improve the quality of housing and you could save all those layers. You could cash out all those layers of bureaucrats between us and count those as the savings.

I'd be delighted to have the challenge. Thank you very much.

Mayor SCHUNDLER. Absolutely, I believe we have the staff to manage that money.

I might add that there would be more money to manage if you got rid of the Federal and the State take in this whole business.

I think, again, if we had the opportunity to manage that money, not only do we have the capacity, but we are under so much more pressure to use that money effectively than you could imagine.

The front page of my local newspaper today, the headline is I hired two people on my staff because there is such a vehement outcry against waste in our Government.

I'm proud that our budget is lower than 3 years ago in Jersey City. Is the Federal Government's? No. Is the State government's? No.

I could tell you that when Federal and State spending goes up, none of my Jersey City residents actually go down and protest at the capital building or here in Washington. But if we were to increase spending by a penny in Jersey City, they'd be all over my—city hall.

[Laughter.]

The bottom line is not only do we have the staff, but we're the ones who are held most accountable. We are the closest to the people.

So the real issue is how do we serve the people? Then give the power to serve the people to the very individual or the very level of Government that the people can control themselves. We are that level.

It would be far better to even cut us out of the pie. Then, again, if we went towards a system of earned income tax credits, that's direct empowerment of the citizens.

I would point out that the 10th amendment doesn't just talk about the States. It talks about the citizens themselves. And if we could directly empower the citizens and take out the bureaucratic take of Government all together, that would be best of all.

Mayor ARCHER. Senator Mack, I would offer the view that block grants, if it is going to be something that's done, should come directly to the large cities.

The States, on the other hand, perhaps after discussion and dialogue and debate, would best be able to administer it for villages, townships, small municipalities after debate within this body to determine at what level of population, if you want to cut it off at population base.

But I do believe that block grants ought to come to large cities.

Next, I would offer the opinion that, at least speaking for my own administration, we are reinventing our city in terms of how we are working.

We are utilizing turn-around teams which is a business concept as opposed to reaching out quickly to privatization. We've chosen to utilize turn-around teams much like business has. And we've also used goal-based governance, which we're working on presently, and total quality management within our city employees, numbering something like in excess of just over 17,000 people.

So my administration will be able to monitor it and would be able to handle it.

I differ from Mayor Goldsmith, and that is, don't take any of my money. I want 100 percent of all of it. Take it from somebody else. You give me my 100 percent.

[Laughter.]

Senator MACK. Do the two of you recognize as well maybe there is a level of certain-sized cities that probably would not have the resources and therefore, the fund ought to be carried out by the States?

Mayor SCHUNDLER. I was going to say, in New Jersey, as an example, there are counties where you don't have cities and so the county government actually does a lot of these services directly.

Most of the things that are done by county government elsewhere in New Jersey is done directly by the city of Jersey City. And I think you would follow that same principle.

Local government does not mean the city itself always. Local government may be in many instances a county government because of the more rural nature of the area.

Mayor ARCHER. Senator Mack, one thing that I did not mention and I beg your indulgence just to make two points.

The first is FHA, it really is doing a fine job and it ought to stay as it is. Don't let anybody privatize it. I would ask you to take a look at that area if you have not done that.

I think it's very important. It provides home ownership and it does it in a very nice way. It, frankly, I think, delivers on the public policy region for which it was intended.

Then, second, I know that you're personally concerned, I believe, over the Community Reinvestment Act as it relates to banking. And I know that you're investigating that.

I'd ask you to visit with Mayor Mike White in Cleveland. Find out what he's been able to do by working with his banking institutions there and how the banking institutions have really used the CRA by working together with Mayor White and his administration to build economically Cleveland, to make it a real competitive city again.

So, it is not a tool that people are being beat over the head with. It's an encouragement tool.

If you do a Nexus search around the country and find out how some cities have been redlined on mortgages and loans and things of that nature, it is an absolutely important tool.

So I would ask you please to give due consideration to that and find out what's going on out in the real world, not that you're not

in it here, but I'm just simply saying find out how we're practically able——

Senator MACK. We are not in it here. I can assure you.

[Laughter.]

Mayor ARCHER. How we're practically able to work with our financial institutions. I think it's an excellent tool.

Mayor GOLDSMITH. Senator, would you mind refereeing a debate here for just a minute?

Senator MACK. No, that's fine.

Mayor GOLDSMITH. This will only take a minute.

Too often——

Senator MACK. That is, unless Mayor Archer wants to respond.

Mayor GOLDSMITH. I'll try to make this slightly a small-scale debate.

I think it's very important to differentiate. In this downsizing atmosphere, I believe that two issues get mixed up.

One is what is the responsibility of Government? What do we want to provide as a service? Do we believe that people ought to have some minimum standard of shelter? Probably most of us would say yes.

That's very different from who should produce that shelter. Should it be a public housing authority, a private sector developer? Does FHA have to be public or private?

I would urge the Senate to separate those issues because it may be in Detroit that, with a great mayor which they have, they can produce things through the public side better than they can the private side. And it may be that certain issues are better produced private than public.

But I think that to entangle those two issues, what's our responsibility to provide from how do we produce it, are very different issues, and I'd like to kind of separate them because, at least from my perspective, we can produce more value in different configurations, not necessarily assuming that a Government delivery system is the best way.

Mayor ARCHER. Let me just say that I do not disagree with the four corners of what he has just said, while not adopting his opening statement and the other things that he's been talking about.

I will say that one of the things I'm grateful for, that the Senate has maintained its integrity in terms of providing an opportunity for this discourse, something that was not provided in the House in terms of no opportunity whatsoever for debate.

I am satisfied, reasonably satisfied with the level of interest that I've seen here today and with the Senate's ability, I believe, to look at what is in the best interest of American people, putting aside who's a Republican, who's a Democrat, who happens to be in the majority, who happens to be in the minority, pass this and pass that. But focusing on what is in the best interest of the American people.

I think that we can get to what Steve and I both want because I think there can be, through that discussion, how can we have the most flexibility to make what happens best for Indianapolis to make it happen, encourage it, and what may happen through either public or public/private partnership in the city of Detroit or

Jersey City or some place else. And you don't have to have all kinds of different regulations all over the place.

I think by listening, as you're kind enough to do today, and your colleagues have because they've been doing other things with other committees, if you do that, I think the American people will win. If it just cuts off with no debate, then I think the American people will behind the eight ball. I don't think any of us want that.

Senator MACK. Let me just expand a little bit now on, again, the concept of if we go this route of a block grant.

Naturally, if you were in our situation, in our positions, there is the natural question of accountability. If we're going to provide the money, there's got to be some kind of assurance that it's going to be done correctly. I guess what I'm asking you all is to give me a sense about how you think we write both maximum flexibility into a block grant and at the same time, accountability.

Do you want to start, Mayor Archer?

Mayor ARCHER. Senator Mack, let me just make it as simplistic as I can.

I'm a lawyer. I'm a former Justice of the Michigan Supreme Court. The only thing I've ever had in my professional career aside from being a teacher is my integrity, my word. The buck stops with me and my administration. I do not want any scandal. I don't want anything going on in my administration over which I have any kind of control.

I will dot every I, cross every T that I have to to make sure that any dollar that comes to the city of Detroit is accounted for.

That's my word to you and that's the kind of thing that I believe all mayors will do.

We will set up, and we already have set up within our administration, I assume other mayors have a similar kind of thing, where we've got the ability to make the accountability happen. Where we need to make changes to accommodate that, we're willing to do that and absorb it, even at our own cost and not a cost to the program, to make that happen.

Senator MACK. Maybe I need to be a little bit more specific. And I appreciate your comments. But I think you would recognize that there can be and have been situations where money that has come from the Federal Government has been misused.

Mayor ARCHER. Sure.

Senator MACK. Again, the question is how do you establish those objectives that I referred to early in the day? How do you write them in such a way that they provide flexibility, but at the same time the recognition of accountability, I guess, if you're not using the funds to meet those objectives?

Mayor SCHUNDLER. I think it becomes fundamentally very difficult, which is one reason why, again, if you went towards individual empowerment where you gave someone an earned income tax credit where they can buy their own housing, then you don't have to worry about that. They earned that money and it's fine for them to go out there.

All you're doing is netting up their income so low- wage earners can actually live decently. And then you're letting the free market provide the housing.

But when you begin—we're going to write block grants and we're going to say—very broadly, we're going to say this is how you're going to have to use this money. And what's immediately going to happen is that somebody is going to be creative at the local level and say, well, it would work so much better if we just did it a little bit differently.

You're going to say, well, that's not quite right, and so you're going to write more regulations to further circumscribe freedom.

What ends up happening is you see an eventual drift back towards more and more regulation if the tide changes slightly and we're back where we started from.

I think you have to get it into your mind from the get-go that if you don't go towards the kind of more grand reform that I've talked about with that workfare and tax credits, I think you have to get through is that what you're really doing is you're block-granting money that the cities can use in the way that's best.

Once you send it down, it will be in our audited statements and if somebody actually absconds with that money, they'll go to jail.

But the fact is the taxpayers will be the ones who are the accountability mechanism for ensuring that that money is spent for the maximum benefit for the community.

To give you an example, I'm sure there's lots of concern here that if you block-grant money to cities, they may use it to lower their property taxes.

I would argue that that may be what they need to keep from losing the bulk of their housing. We have a lot of cities in America where the property taxes are far higher on a real value basis than they are in comparative suburbs.

So what we have is we have not just—middle class flight has already occurred in many cities. Now you've got working class flight. And you've got some cities where they're on the verge of being purely those who cannot afford to leave.

It may be that what a city needs most is property tax relief until you have far more housing preserved for low-income Americans by virtue of giving them their freedom.

The minute you get in there and start writing regulations to try to specifically say that it has to be done this way, you're going to find that there is the temptation to try to be more creative because that's actually what they need at the local level.

If you trust in the people, then you don't have to go to work late at night—I should say you don't have to go to sleep late at night worrying about whether we've spent the way you've said.

The people will make sure at the local level that's it's spent the way that it actually helps the most.

Mayor GOLDSMITH. Yes, I think just a footnote, Senator

Again, we're trying to create wealth and stabilize our population base.

I think your question is an insightful one because it pushes on a not easily resolvable tension. You have a right to hold us accountable. But the more you write in performance standards, the more perverse the activities as they get down to the lower level.

I don't mind. Too often the Federal Government writes input standards rather than outcome standards with the performance standards.

We could debate what those might be. However, I think I would take the last statement and suggest simply that when the Secretary proposed a separate fund for homeless, that struck me as curious because I'm the last repository of shelter for the homeless.

So why are we differentiating public housing fund, a homeless fund, and several other funds, even within the block grants as the Secretary proposed?

Insofar as my voters and the citizens hold me ultimately accountable for shelter. And if I'm spending your funds for shelter for people below some sort of defined poverty level, I think that that's all the accountability that you should require because the more you push from the top down, the more waste there will be through the system as they try to circumvent the rules.

Senator MACK. Again you recognize the concern that some would say—I assume if they were here they would say—that some cities, some States, would not be sensitive enough to specific areas that have been identified by the Secretary needing special attention.

And again, we get into that fundamental question about objectives and accountability.

You wanted to say something.

Mayor ARCHER. I just wanted to make this one point, and I know that we're treading at the bewitching hour of 12:30, which was in the letter that you mentioned.

Senator MACK. We're going to go a little bit beyond that, if you all can stay.

I know that Mayor Goldsmith probably has to go.

Mayor ARCHER. Let me just make the following observation.

The Mayor to my right speaks eloquently about property tax relief and the like. But I think you miss a fundamental point. And that is that you must have the money to pay the property taxes, whether they're low or high.

So what we're doing is trying to create a housing environment for people who have low-income.

My desire is to move people up and out of poverty. I'd like to see them move up and out, save for senior citizens, who are no longer in the work force, I'd like to get the younger people up and out and into other housing and have an opportunity for people to have transitional housing.

I'm looking at jobs, economic development and the like. And I know that we can make that happen in the city of Detroit.

But we need to have—for example, in Parkside, which was a grant that was made out of the Hope 6 grants where it is now cut off by rescission, $47,674,000.

We've got planning going on right now because we were given the grant. We started working on the process. You go across the street to Parkside housing, you'll see a building over there where people have been coming in, parents and children, children weighing in and saying, this is what we'd like to have here.

We're looking at greenspace. We're talking about doing it in a manner in which I think it was purposely intended.

I would say that in terms of public housing, I'm not afraid of the vouchers at all. I think there ought to be a challenge. You give the money to allow us to make the improvements that ought to be made, I'll test that market.

I'll tell you one thing that I don't think is going to happen, is that I don't think that you're going to find any invitation going from our suburban communities to giving Section 8 voucher folks to go out to our suburban communities because most people who are in public housing are going to be viewed as different and therefore, not going to be readily acceptable.

We need to have the opportunity within our cities to solve the problem. We can do it if you give us the tools.

Mayor SCHUNDLER. Senator Mack, if you go and speak to the people of Jersey City and say, what are the most important services that Government can provide, they'll talk about police, they'll talk about schools, they'll talk about fire. Now who do you think provides that?

Then if you go and you look at where they're tax dollars are going, who do you think takes the majority of their tax dollars?

The Federal Government takes by far the larger portion of Americans' income. The State government takes a little bit less and then the local government takes a little bit less.

Yet, we're the ones again who have the people all over us for making sure that we're spending the money well.

I would argue the real issue that we have to ask the Senators and the Representatives is how can we possibly hold you accountable when you're this far removed from the people?

You've got all this money that you've taken away and it's not accessible to us for the things that the people really want.

We would like to try to improve our schools. We'd like to try to improve so many things about Jersey City, but there's no money out there because it's all been taken away by more distant governments which are less responsible and less responsive to the people.

Just to again provide a little example of this.

We have exclusive neighborhoods in Jersey City where they have a wall around them. They have a call on police services if they need police there. They also get garbage pick-up and the various sanitation services that the city provides.

On top of that, they assess themselves a little bit of extra money and they have private security guards and they have private outdoor maintenance companies. Actually, you have these beautiful flowers growing in front of everybody's house. They don't even water it themselves. They just have folks come by and keep their own garden beautiful all the time.

Now why is that only in the exclusive neighborhood? Why can't I go into my lowest income neighborhood where I've got so many people who are unemployed? And why can't I put people to work right in that neighborhood providing supplemental security at a much lower cost than what it costs to hire a policeman?

Why can't I have a private company doing outdoor maintenance so the streets are clean? I've got these people who need jobs and they're getting money right now from the Federal Government not to work.

Now that is very irresponsible Government. I think it's time we hold the Congress accountable.

Senator MACK. I wish my colleagues were here.

[Laughter.]

I don't mean to defend that.

Mayor ARCHER. How do you like all this weight on your shoulders, Senator?

Senator MACK. Again, I recognize that you have to go and I just have one other thought I want to toss out and if you need to go on, go right ahead. I appreciate your being here this morning.

Mayor GOLDSMITH. Thank you very much. Thank you.

Senator MACK. It kind of touches on what Mayor Schundler has raised.

If I'm not mistaken, what you're really talking about is the proposal that Professor Friedman put out years and years ago, the negative income tax.

Mayor SCHUNDLER. Except there should be work required at the end of that.

Senator MACK. Yes. I understand. One of the thoughts that's occurred to me as I've gone through these different hearings, not only in the authorizing committee, but in the Appropriations Committee, is I keep thinking of this from the perspective of why aren't we organizing whatever assistance we're providing, why don't we do it from, in essence, the customer's perspective instead of the Government's perspective?

The Government's perspective is, as has been raised here, is that there really are a whole series of different ideas that each one of us up here has as kind of a pet project. And before we know it, that pet project becomes part of the overall bill. And it's specially designated and specially set aside.

That's just within one department. That's within HUD.

I just want to go back to—let me find it. HUD is in the business of fair housing, protection of vulnerable populations, job training, economic self-sufficiency, deconcentration of low-income families, coordination of housing and social services, in addition to affordable housing, home ownership and community development. I could go on.

But then you can go into each different area of the Federal Government, different agencies who have either similar responsibilities or additional efforts that they're involved in to provide assistance to those people we are deeply concerned about.

I keep wondering, why don't we bring all of this together in one department, one agency, one effort, and then build what we need to be doing for that individual from the grassroots up, not the top down?

Mayor ARCHER. Senator, if I had to guess, I would believe that the reason why you have HUD focused as it is, and it's viewed at least by the mayors that I've met since being the Mayor of the city of Detroit on January 1, 1994, HUD is viewed as the Department in which we as mayors of cities can go to on issues dealing with the city.

As you've indicated in terms of looking at the parameters of what HUD says it takes care of, and it really does, there are other different departments in the Federal Government that have similar kinds of programs.

I think what you have just said in your own statement has provided the answer. And that is, someone who knows of a need, can't fit it into HUD, finds a bill on which they can tag it onto, puts up

an amendment and the next thing you know, because they're an advocate for it, they're able to convince their colleagues of it.

Then you've got an ancillary program in another department that is doing some of the same things crossing over some of the same parameters as a principal department does.

If I could just respectfully suggest the following.

One of the things that you have clearly demonstrated your interest in this day, and I've been singularly impressed, as I was when we first met, is that if I can encourage you to consider part of your summer, since this is not an election year, of having some of your colleagues pick different parts of the United States that would give you a taste of the customer of which you spoke, and have some Senate hearings where you could gather some information.

If you can't do that because of the press of demands, then send some of your senior staffers out that you have faith in and that has the sensitivity, on the same wavelength, you trust their judgment.

Why not gather some Senate staffers and send them out and have them listen, have them dialogue, interface with me or interface with my director of the housing department that I got from Sacramento, California, or Carl Green, who I got away from Atlanta, Georgia, to come in help solve the horrible problems in——

Senator MACK. I'm not sure I want you to get to know my staff. [Laughter.]

Mayor ARCHER. But if you did that, I think you would find a theme, a common thread in terms of how to deal with the issue and then as you're listening and asking, well, what are the departments that you can begin to identify from your customer base, from your local customer base, local government, or at least listening to people who are in the trenches, the Community Development Corporations, who are actively involved in our neighborhoods and the like, they could just give you chapter and verse of the horrendous problems that they've had in the past.

What I think they would say now, they see some improvement and how we can even do it better.

I think that that would provide you with the information that you need and the comfort level in which to then take a look at, how do we best deal with this thing and how do we help make this—because, see, if you work together in a bipartisan way and the focus is always on what's in the best interest of the American people, whether you divide it up and say, what's in the best interest of the homeless of America? What's in the best interest of the low income? What's in the best interest of our wealthiest? How can we generate more opportunity for them to create wealth so that others coming below them will be able to find the jobs that they're going to create?

If we were to do that, just sort of take our time and not rush through things, I think you'd find the key to that.

Mayor SCHUNDLER. Senator, I think your question is extremely on target and it's the exact kind of question that we should be asking ourselves—why have we done it this way?

I think it's because of the desire to feel good, because giving makes one happier than receiving.

I think in Congress, well intentionally, they thought that if we could do this for people, that would be a good thing and then I feel

good about myself. So every Senator and every Congressman for the last 50 years has been proposing, let's do this, let's do this, let's do this.

But, again, you talk about person-focus. We have to think, well, what makes each of us feel good?

I don't know of anybody who wants to be a coma victim. But think about it—you lie on your back all day. They feed you. You don't even have to walk. You don't have to breathe on your own. Everything is done for you.

But nobody I know wants that. Everybody I know wants to walk on their own feet. And they want to not only take care of their own family. They want to be able to do good for others again.

Man doesn't live by bread alone. We get a sense of purpose when we're able to do for ourselves and to others and be independent.

That's what our real focus has to be. We've been taking these approaches of entitlement where we say, we are going to give you a house. And what we do—the housing projects in Jersey City were originally built for returning veterans from the Second World War.

Materially, it's not bad housing. But spiritually, those are places of anomie because there's a lack of purpose. Young people go into drug dealing because, again, they're cut off from real educational opportunity with our Government monopoly system, cut off from the sense that you can actually achieve on your own because of the experience that they're witnessing, work and so forth.

These are folks who are lost. What you end up with is social problems. The housing is not bad. But the social problems that prevail make it an unpleasant place for people to live. And so they'd sooner not be there.

Now I've never met a person on welfare who wants to be on welfare. I haven't. Every single person I've met on welfare, and we've got 13,000 AFDC families in Jersey City. Every single one of them wants a job.

If we do take a person-focus, we begin that real review, instead of just tinkering at the edges. What we'll say to ourselves is what we have to do is make sure that every person who is willing to work can get a job and somebody who's not willing to work shouldn't be assisted.

We should not subsidize that lack of self-responsibility. We should challenge them to be responsible and we should empower them to be able to earn what they need. That's why I've talked about the program I've discussed.

I think something we do have to realize. Sometimes we Republicans talk about a job being the best social program, which is true. We imagine that if we're able to lower taxes, that there won't be a need for some type of backdrop job, if you will. The private sector will provide all that is necessary.

The reality is that capitalism is creative destruction. We will see an acceleration in the development of technology and, I might add, dislocation as we are able to create a more productive economy.

The lower we put taxes, the more capitalism thrives, the greater wealth that's created, the more dynamic and vibrant the economy, the more we'll see economic dislocation. Industries will be born and they'll be dead in 5 years and made obsolete.

So there will have to be a need. There will have to be an opportunity for someone who was working and suddenly is without a job, to know that tomorrow they can still go and find work.

Again, from my perspective, there's so much to be done. There's no problem for us making sure that there's something, that it's actually constructive and provides something back to the community in exchange for the guaranteed income that we're going to provide.

But that's the focus. Let's make people whole. Yourself, myself, Mayor Archer, none of us ever aspired to be on the dole. All of us aspired to be able to be contributing members of society.

We should make sure that that's a realization for those who desire it who currently have been shut out.

Senator MACK. Well, once again, I appreciate your coming here today and providing us with your thoughts.

In particular, I will consider your challenge, in essence, to get out in different communities. In fact, what I think I'd like to do is maybe ask both of you to kind of give some input as to how I would spend my time if I came to your city.

Mayor ARCHER. We'd love it.

Senator MACK. And see if that is something that we could work out. Again, thank you for coming.

The meeting is adjourned.

Mayor ARCHER. Thank you very much, Senator. We appreciate it.

[Whereupon, at 12:43 p.m., the hearing of the subcommittees was adjourned.]

[Prepared statements and additional material supplied for the record follow:]

PREPARED STATEMENT OF SENATOR ALFONSE M. D'AMATO

Chairman Mack and Chairman Faircloth, I would like to commend you for holding this Joint Subcommittee hearing to discuss the operation of the Department of Housing and Urban Development and proposals for the agency's future. Today is the second of a series of fact-finding hearings to analyze HUD's current mission and degree of effectiveness, and to determine its future.

It is imperative that Congress, HUD, local and State governments, and the housing industry work together to make Federal housing and community development programs work better for those they are intended to serve. Given the increasingly tough budget restraints, it is vitally important that we fulfill our responsibility to the American taxpayer to ensure that every Federal dollar is maximized to its greatest potential.

On March 20, the Administration released a document entitled "HUD Reinvention: From Blueprint to Action." This document is the successor to HUD's "Blueprint" which was released on December 19 of last year. I commend Secretary Cisneros for his strong commitment to reforming the Department, and applaud many of the principles of his reinvention—such as consolidation of programs and deregulation. However, many questions remain to be answered. I look forward to hearing the Secretary's testimony and am hopeful that it will outline HUD's proposed changes in greater depth.

Despite years of efforts to revitalize HUD, serious management problems continue to plague the Department. Last year, the GAO designated HUD as a "high-risk area" because of four longstanding Department-wide deficiencies. HUD has made marginal improvements, but effective management must continue to be the top priority for the Department. Without proper management, any attempts to reorganize HUD will be fruitless. The serious systemic problems must be rooted out, once and for all.

The Banking Committee and its Housing Subcommittees will be diligent in evaluating HUD's recommended "reinvention" and proposals for its elimination. Every aspect of HUD will be scrutinized. HUD is expected to do too much and has too many varied and competing constituencies. We must determine which current functions should be transferred to other Federal agencies or other levels of Government and which programs, if any, should be preserved within HUD.

I am certain that the end result of this hearing process will produce major legislative and regulatory changes affecting HUD, but that is not our central purpose. We must not forget that our fundamental goal is to address the affordable housing and community development needs of our citizens.

Responsible legislation requires a great deal of time and consideration. I look forward also to hearing the views of our Nation's most prominent mayors. I am hopeful that Congress, HUD, and our Nation's local and State officials can work together on a bipartisan basis to assess the future of the agency and to guarantee that the housing and development needs of our citizens will be achieved in a better managed, more cost-effective way.

PREPARED STATEMENT OF SENATOR CHRISTOPHER J. DODD

In my statement at the first of these hearings earlier this month, I noted the importance of maintaining an efficient Department of Housing and Urban Development (HUD). I do not want to repeat myself here, but the point is critical. The Federal Government cannot walk away from its responsibilities to those citizens struggling to build a better life in the troubled communities across this Nation.

There are still too many neighborhoods, particularly in our urban areas, where living conditions are unacceptable. All of us have seen the abandoned buildings, the garbage and graffiti, and the people living on the streets with little hope for a better future. We owe the children in these neighborhoods—the kids who have turned away from drugs and gangs—an opportunity for a productive, hopeful life.

And there are hard-working people, even in the very worst neighborhoods, who are struggling to turn their communities around. In my home State of Connecticut, citizens are working with church and community groups, neighborhood patrols, and other organizations that are reclaiming and rebuilding communities block by block. The Federal Government must support, not abandon, such efforts.

Today we have Secretary Cisneros with us—someone who knows the problems as well as anyone. Although he inherited a Department plagued by problems ranging from mismanagement to outright corruption, he has made significant strides forward. By streamlining programs and cutting back on the bureaucracy, he has made

HUD a more effective partner for local communities. I commend him for those efforts.

Clearly, more needs to be done to improve HUD. This hearing will help move that process forward. Secretary Cisneros has submitted a proposal for improving HUD and its programs, and I look forward to reviewing those plans with my colleagues. We need to get a better sense of the details of these changes, the way they will be implemented, and the effect they will have on residents of public and assisted housing.

In the past, the Senate Banking Committee has worked in a bipartisan manner on housing issues. During the last Congress, we worked together to pass the HUD Demonstration Act and the Multifamily Housing Property Disposition Reform Act. These measures provide HUD with additional tools and flexibility to rebuild communities.

Hopefully, we can continue on this bipartisan path to reform. However, I continue to have concerns about the severe cuts to housing programs, or the outright elimination of the Department, that some of my Republican colleagues have proposed.

The rescission package passed by the House contains more than $7 billion in cuts from HUD programs for Fiscal 1995. As set forth in my last statement, these cuts would have a devastating effect on communities across the country.

Although the Senate Appropriations Committee proposed a lower level of cuts from housing programs, about $4.6 billion, those cuts would still take a terrible toll. The cuts in rental assistance could force families with children, and elderly people, on to the streets. The cuts in modernization for public housing will lead to the further deterioration in these developments—we'll have more vacant buildings with boarded-up windows. Of course, this kind of cut also means a loss of jobs—particularly in the construction industry.

Today we begin debate on the Senate floor on these proposed cuts. I will work to prevent these cuts and I urge my colleagues to join that effort. We need to continue down the road to responsible reform and not adopt drastic measures that jeopardize the living conditions, and jobs, of thousands of families across the Nation.

STATEMENT BEFORE THE SENATE BANKING, HOUSING AND URBAN AFFAIRS SUBCOMMITTEES ON HOUSING OPPORTUNITY AND COMMUNITY DEVELOPMENT AND HUD OVERSIGHT AND STRUCTURE

MARCH 29, 1995

By

SECRETARY HENRY G. CISNEROS

Senator Faircloth and Senator Mack, thank you for inviting me here this morning. I appreciate the opportunity you and the Members of your Subcommittees have given me to discuss our proposals to reinvent the Department of Housing and Urban Development.

Three months ago, President Clinton announced an ambitious proposal to reinvent HUD. Nine days ago, we sent Congress a detailed plan for translating the President's Reinvention Blueprint into action.

This morning, I would like to briefly outline the principal components of our reinvention plan, and answer some of the main criticisms of our plan, and I welcome the opportunity to answer your questions about it.

In summary, our reinvention plan has three components:

- Consolidation of 60 major programs with separate appropriations and application procedures into three, broad, flexible funds for localities and States. Some additional 180 set-asides, activities, and inert programs will either be consolidated into these three funds or permanently retired.
- Revolutionary changes in public housing which will empower residents and infuse market discipline into Washington's relationship with public housing authorities and will give residents real choices that bring dignity to their lives.
- Transformation of the Federal Housing Administration into a streamlined, entrepreneurial, Government-owned corporation to promote home ownership on an unprecedented scale.

Consolidation: Simplifying and Decentralizing Assistance to Communities

A key element of our reinvention plan is program consolidation.

I'd like to draw your attention to the chart which summarizes this consolidation and which makes it easier to visualize how it will occur over the next 5 years or so. We are ultimately consolidating 60 separately funded, specialized programs into three funds. This consolidation also covers some 200 other HUD activities—literally a hodgepodge of active programs, inactive programs, set-asides, technical assistance funds, eligible activities, regulatory functions, and insurance authorities. The bottom line is three funds:

First, the **Community Opportunity Fund,** to stimulate community revitalization. All current HUD grant programs for community development and job growth—including Community Development Block Grants (CDBG) and Economic Development Initiative Grants—will be consolidated into this fund, which will give localities and states broad flexibility to stimulate business growth and expand job opportunities in economically distressed communities. Funds will be allocated like CDBG—70 percent to localities and 30 percent to States.

Second, the **Affordable Housing Fund,** to support production and rehabilitation of affordable housing. All current HUD programs for development of housing for low- and moderate-income families and individuals will be rolled into this fund, which will be administered by local and State governments. This fund will use the HOME allocation system—60 percent to localities and 40 percent to States.

Third, the **Housing Certificates Fund,** to provide direct assistance to low-income households for affordable rental housing and home ownership. All current public housing, assisted housing and Section 8 rental assistance programs will be combined into this fund, which in most instances will be administered by public housing agencies.

Program consolidation will result in significant downsizing and streamlining at HUD. But it is about more than cutting HUD bureaucracy and red tape. It is about enabling communities to use Federal resources more effectively in combination with their own public and private resources. I'd like to take just a moment to talk about how consolidation will make a difference for localities and States.

- Consolidating scores of often overlapping, competitive programs into three performance funds will make it much easier for localities and States to obtain Federal resources, and it will give them much more flexibility in using these resources.
- Consolidation will enable localities and States to develop and implement comprehensive plans to strengthen communities and help people lift themselves. Instead of demanding dozens of separate funding applications for a panoply of competitive programs, we'll ask for a single application, with a single, consolidated plan for affordable housing and community development. Communities will have access to the latest technology, enhancing citizen participation as well as local decisionmaking.

Communities will be able to develop a vision and pursue long-range strategies to address **their** needs.

- Consolidation will support the vital work of more than 3,000 community development corporations that are producing housing and providing services for low- and moderate-income people in cities and rural communities across America today. We will build on their success by directing 30 percent of the Affordable Housing Fund to nonprofit community development organizations—an unprecedented commitment of Federal resources to this critical sector.
- Consolidation will reward performance. We will establish bonus pools in the Community Opportunity Fund and the Affordable Housing Fund. Communities that successfully use their formula grants to promote job creation and expand affordable housing will be able to compete for additional funding, and they will be given greater flexibility.
- Consolidation will enable localities and States to improve and rationalize their efforts to reduce homelessness and provide housing for people with AIDS. Most significantly, HUD's six separate McKinney homeless programs will be immediately consolidated into one, flexible Homeless Assistance Fund, enhancing the ability of localities and State to fashion comprehensive and coordinated strategies.
- Finally, consolidation will result in increased housing and job opportunities for Native Americans. Under our reinvention plan, all Native American programs will be merged into one office, and set-asides for Native Americans will be increased under the Affordable Housing and Community Opportunity funds. This will mean $172 million more for Native American housing and community development in fiscal 1996.

Our consolidation plan has been criticized for not giving localities and states enough flexibility. Some have suggested that we just send money—no questions asked. But we cannot allocate tens of billions of dollars without setting standards. To say, "anything goes" is a blatant invitation to fraud on the one hand, and complete lack of accountability on the other.

But setting standards does not mean tying localities and States in bureaucratic knots. We can have standards and flexibility.

We propose a two-tier system of accountability and performance. Localities and States will first have to comply with minimum statutory requirements such as low-income targeting and fiscal accountability. Jurisdictions will also set performance measures which reflect national goals and objectives, such as job creation, increased home ownership and moving low-income families to self-sufficiency. Bonus funds will be made available to those localities and States that comply with the minimum requirements and then meet or exceed their performance measures.

We'll ask localities and States to show us, in their consolidated plans, how they intend to address these national goals and objectives, and we'll ask them to set their own benchmarks by which their performance can be evaluated. And then we will reward performance with bonus funding and increased flexibility.

Power of Market Discipline and Individual Choice: Public Housing Transformation

The second component of reinvention is to radically transform public housing in this country.

Public housing's problems are structural and systemic. Our proposal for transforming public housing is simple, yet profound—because it cuts to the heart of these problems. Where the current system gives public housing agencies subsidies to maintain projects, we would give families housing certificates—which they could use in public housing or a private apartment of their choice.

If they don't like the housing offered by housing authorities, they will be able to move. Housing agencies will have to compete for their business, just like private landlords. Well-managed authorities will survive; poorly run authorities will have to shape up or go under.

We have proposed other far-reaching changes.

- We would allow PHA's to issue up to half their certificates to working families and families preparing to enter the workforce. Current preference rules have turned public housing into weak and unkept warehouses for the very poorest of our fellow citizens. In 1980, the average household income of public housing residents was 33 percent of area median income. By 1992, it had declined to 17 percent. Changing the rules to admit more working and work-ready families will return public housing to its original purpose as a first step on the ladder of self-sufficiency.
- We would change rent rules, to make work pay and encourage working families to remain in good public housing. Every expert believes income integration is essential to good property management. Yet, public housing residents tell me they actually have less disposable income after they go to work than they had before,

because of sharp rent increases. And working families are often charged rents that are higher than market, since rents are based purely on income. We will change the rules to allow public housing agencies to set ceiling rents as well as help families make the transition to employment.

- We will support increased involvement of residents in public housing management.
- We will require all able-bodied residents of public housing who are not employed to perform 8 hours of community work a month.
- We will eliminate the one-for-one replacement rule which requires public housing authorities to replace every unit they tear down with a new housing unit. Since 1987, this rule has made it virtually impossible for public housing authorities to tear down deteriorating, mostly vacant buildings, which continue to blight inner-city neighborhoods. Shifting to a system that relies on certificates will open the way for these units to come down.
- We will also substantially improve the utility of Section 8 rental certificates. Rules that have impeded the participation of good landlords—such as the requirement that landlords who rent to one Section 8 family must open all their units to Section 8 families, the so-called "take one, take all" rule—will be eliminated. Families will also be able to use certificates to purchase a home. Certificates are now used to pay debt service to private landlords; why not allow families to use these subsidies to support their own mortgage payments.

Clearly, changes this fundamental cannot be accomplished overnight. There are 1.3 million households now living in public housing and 3,400 agencies managing this inventory. We propose an orderly and prudent transition to prepare agencies and residents for the shift to a market environment.

Small public housing agencies will convert to the certificate model by the end of 3 years. For larger PHA's, there will be a 6-year, three-part transition. During this time, good public housing will be brought up to market standards, and nonviable stock will be torn down.

- During the first transition stage, beginning in fiscal 1996, HUD will consolidate dozens of disparate public housing programs into two accounts, one for capital and management improvements, and one for operations. The Nation's 3,300 well-performing public housing agencies will be able to modernize units which are worth improving and to tear down units that are not worth saving.

During this time, HUD will focus its full attention on the 100 agencies that continue to exhibit severe management deficiencies. We will seek new, enhanced receivership powers, and intervene aggressively to turn these agencies around.

- In the second transition phase, existing capital and operating subsidies will be converted to project-based assistance, and agencies will learn to operate under market discipline. Rental income—instead of arbitrary capital and operating budgets—will drive their property-management decisions.
- In the final phase, all subsidies will be converted to tenant-based assistance.

Some of our critics don't want to change the current public housing system. They say we've gone too far. They say vouchers can't work, and that the current system works well enough.

But our experience—over the course of 20 years of running voucher and certificate programs—shows that vouchers and certificates do work.

Fully 80 percent of the families involved in these programs in large urban areas today have been successful in finding housing. Nationwide, there is a substantial supply of housing available at or below the fair market rents supported by Section 8 assistance, and it is widely dispersed throughout our metropolitan areas. And, remember, a substantial portion of the public housing inventory will be upgraded—and many residents will use their vouchers to remain in their existing apartments.

The housing **is** there, and people **can** successfully use certificates to obtain this housing.

Furthermore, we can empower people to make choices at significant savings to taxpayers. The average appropriation per occupied unit of public housing is $481 a month, compared to $440 a month for rental certificates.

In short, we would move to a system driven by consumer choice and market discipline. This new system gives residents real choice about where they live and engages them in the management of their housing. That empowerment of residents will bring more pressure on housing authorities to maintain, repair and secure developments than a building full of Federal regulators could ever hope to apply through traditional memos, cautions, sanctions and declarations. The infusion into the system of this choice for residents—to vote by leaving—will change public housing more profoundly than any other action since its creation.

An Entrepreneurial, Results-Driven FHA: Built for Record Home Ownership

The Federal Housing Administration's historic mission has been to help average, working Americans become homeowners.

We are proposing to completely recast FHA. We want to transform it from a slow-moving bureaucracy into a streamlined, market-driven, Government-owned corporation which will expand home ownership to more low- and moderate-income working families and boost our national home ownership rate to an all-time high by the end of this century.

The new Federal Housing Corporation would rely increasingly on partnerships with well-capitalized, sophisticated financial institutions, including Fannie Mae and Freddie Mac, the Federal Home Loan Banks, private mortgage insurance companies, State and local housing finance agencies, and community-based organizations, to design a variety of products that meet market needs and share risk.

Performance goals would be set to ensure the new FHC's accountability on such measures as meeting the needs of underserved populations, budget issues, and financial performance.

There are some who say we haven't gone far enough. They want us to sell FHA off to the private sector. This would be a terrible mistake. It would undo 60 years of virtually unimpeded progress in home ownership for average working families in America. Look at what FHA does today:

- FHA insures one out of every six new home loans.
- First-time buyers account for 65 percent of FHA's home-purchase borrowers, and more than 30 percent of all first-time buyers are served by FHA.
- FHA insured two and a half times as many loans to African-Americans as all the private mortgage insurance companies in this country put together.

What would happen if FHA were privatized?

It is estimated that 230,000 to 300,000 mortgages would not be made at all if there were no longer a full Federal insurance program. And if FHA were eliminated, the national home ownership rate would decline from 64.6 percent to 64 percent by the year 2000, instead of rising as we believe it can, and must.

As a Government-owned corporation, answering to the American people, the new FHC will continue to serve a vital public purpose—expanding home ownership to lower- and moderate-income working families who are not consistently well served by private mortgage insurers.

The new FHC will, in essence, operate more like a modern insurance company, relying on the latest technology and centralized processing centers to conduct its business. Such innovation will ultimately enable FHC to downsize from its current staffing level of 6,000 to some 2,500 employees.

The new FHC will also have two other critical responsibilities. First, the FHC will continue to play an important role in making mortgage credit for affordable rental housing.

Second, the FHC will address the multiple problems posed by the 1.6 million units subsidized and insured under older FHA and Section 8 programs. Many of these properties are over-leveraged and the Federal Government is paying excessive subsidies to prevent mortgages, from going into default.

We basically have 3 alternatives. On one hand, we could stay the course and continue over-subsidizing the inventory, at a cost of some $64 billion over the remaining mortgage terms.

We could also turn off the Section 8 faucet. Yet this would result in massive defaults and foreclosures, triggering substantial costs to the FHA funds.

Finally, HUD could do what the RTC and FDIC and Freddie Mac and many conventional lenders have done for the past 5 to 10 years—mark to market the debt on these properties to reflect true economic value, ultimately converting all subsidies to portable certificates that support families not projects. This final option clearly makes the most sense from the perspective of the taxpayers, residents, and communities and that is what we have proposed.

Reinvention's Consistent Themes

The essence of our plan is to harness larger forces that can be used to transform a bureaucracy into a modern, entrepreneurial organization. Our reinvention proposals are informed by consistent themes:

- *Simplification, flexibility, and performance.* For example, program consolidation simplifies HUD's procedures, gives localities and States increased flexibility to pursue their own initiatives and builds performance incentives into Federal funding.

- *Individual choice and market discipline.* For example, public housing transformation shifts Federal assistance from bureaucracies and buildings to people and requires public housing authorities to compete with other landlords for residents' business.
- *Managing for results.* For example, the new Federal Housing Corporation will be graded on how well it meets national home ownership objectives. At the FHC, just as with private companies, performance will come first.

HUD Budget

The budget implications of HUD's reinvention plan are significant and real. We have projected 5-year savings of $51 billion in budget authority and $13 billion in outlays, relative to fiscal 1995 program levels after adjusting for inflation.

A substantial portion of budget authority savings come from shortening contract terms for Section 8 rental assistance. The bottom line is that shorter terms will enable the Federal Government to more accurately project the expenditures of rental subsidies, with no discernible impact on residents, landlords or public housing agencies. We have, in essence, been over-budgeting Section 8 rental assistance for years; this can no longer be tolerated in an era of tight constraints.

Savings in HUD outlays are also substantial; outlays will grow at half the rate assumed in the baseline. These savings reflect a dramatic shift toward policies that will impose market constraints on HUD's support for affordable housing. We will end excessive subsidies to landlords through marking-to-market the rents on older assisted properties. We will reduce the fair-market rents for housing certificates. We will change admission rules in public and assisted housing to reward work, so that we move toward self-supporting, mixed-income developments. And HUD's work force will be reduced from 12,000 employees to 7,500 over the next 5 years, saving taxpayers $800 million.

The Case for Effective National Policies to Assist Cities and Communities

In closing, I want to respond to the recommendation by some that the Department of Housing and Urban Development be eliminated.

Eliminating HUD would not reform Federal programs or policies—which all of us agree need restructuring. Responsibilities would merely be spun off to disparate Federal agencies with little understanding of, or familiarity with, housing and urban development issues. This strategy might "hide" the problems under other Federal umbrellas, but real, tangible change in our communities, where it counts, would be stymied.

Eliminating HUD would also transfer the Office of Fair Housing and Equal Opportunity to the Department of Justice. This would upset the careful, constructive bipartisan agreement on fair housing that was reached by the Reagan Administration and Congress some 7 years ago. As Senators Kennedy and Hatch both noted, the division of responsibility between HUD and Justice preserves the historic role of the two agencies in fair housing matters, builds on their expertise and reasonably keeps separate different facets of fair housing enforcement—rulemaking, conciliation of individual complaints, prosecution pattern and practice cases. This Administration fully supports the bipartisan agreement on fair housing negotiated by the Reagan Administration and opposes any effort to remove the Fair Housing office from HUD.

Eliminating HUD would not necessarily save money, Federal or otherwise. The Department now serves 4.7 million households, 35 percent of whom are elderly, and nearly all of whom have very low incomes. The millions of people in these households will still be with us even if HUD is dismantled. The buildings in which they live will remain. The needs will still be acute. These burdens will be shifted onto the shoulders of localities and States that are already fiscally hard-pressed. And at a time, when we are relieving localities and states of the burden of unfunded mandates, we should not be piling new burdens on them.

Retaining a reinvented HUD as the premier Federal housing and community development agency will enable us to coordinate the critical components of a coherent national policy under one roof: The oversight of capital markets, the interplay between Government subsidies and private investment, the removal of barriers to affordable housing, including discrimination, and so on. Keeping all these activities in one Federal agency will promote a creative synergy between them that will leverage and multiply Federal investment many times over.

Our reinvention proposals offer a new path. We have broken the mold at HUD. We have proposed these sweeping changes because only one thing matters out on the streets—making our communities livable and workable again.

Thank you for your patience and your attention. Now I would be pleased to answer your questions.

SUMMARY OF HUD'S PROGRAM CONSOLIDATION

Current Major Programs (60)	FY 1996	FY 1998 & Beyond
Public/Indian Housing Development Public/Indian Housing Amendments Severely Distressed Public Housing PH Major Reconstruction Public Housing Coordinators PH Vacancy Reduction Tenant Opportunity Program Urban Youth Corps PH/IH Modernization Family Investment Centers PH Youth Apprenticeship	PH/IH Capital Fund	Housing Certificate Fund
PH/IH Operating Subsidies Drug Elimination Grants Youth Sports PH Service Coordinators	PH/IH Operating Subsidies	
Section 8 Certificates Section 8 Vouchers Section 8 Contract Renewals Section 8 Family Unification Section 8 for Persons w/ Disabilities Section 8 for Persons w/ AIDS Section 8 for Homeless Section 8 Opt-Outs Section 8 Counseling Section 8 Pension Fund Certificates Section 8 Veterans Affairs Supportive Housing Section 8 Headquarters Reserve Lease Adjustments Family Self Sufficiency Coordinators	Housing Certificate Fund	
Flexible Subsidy Title VI Preservation Program Section 8 Property Disposition Section 8 Loan Management Set-Aside Elderly Housing Service Coordinators Project-Based Service Coordinators Congregate Housing Services	FHA Multifamily Housing Resolution Activities	
CDBG Economic Development Initiative EZs/Economic Development Initiative UDAG Recaptures Youthbuild Colonias Early Childhood Development Neighborhood Development Community Adjustment Planning	Community Opportunity Fund	Community Opportunity Fund
HOME National Homeownership Fund Housing Counseling Elderly Housing (S. 202) Housing for the Disabled (S. 811) HOPE 2 HOPE 3 Lead Based Paint Hazard Reduction	Affordable Housing Fund	Affordable Housing Fund
Shelter Plus Care Section 8 SRO Emergency Shelter Grants Supportive Housing Innovative Homeless Initiative Rural Homeless Grant/Safe Havens	Homeless Assistance Fund	
Housing Opportunities for Persons w/ AIDS	Housing Opportunities for Persons w/ AIDS	

PREPARED STATEMENT OF STEPHEN GOLDSMITH

MAYOR, INDIANAPOLIS, IN

MARCH 29, 1995

Thank you for inviting me to comment on the Department of Housing and Urban Development's "Reinvention Blueprint" and on some of the opportunities for Congress to develop a positive agenda for America's cities without writing bigger Federal checks.

Congress must recognize that the marketplace in which cities operate has changed. No longer do major cities compete against each other for businesses and home owners. We compete against our suburbs, and we start out at a substantial disadvantage. Our suburbs typically have lower taxes, better schools, less crime, and better land for development. As a result, wealth and jobs are rapidly flowing out of our cities, leaving pockets of poverty behind.

My message is fairly simple. There is not enough government money local, State, or Federal—to redistribute in a way that will solve the problems afflicting our urban cores. If America's cities are to succeed, we need to create wealth, not just redistribute it. And the way to create wealth is through the marketplace, not through Government spending.

To put it another way, I need more people in my city, not more programs. The most effective way for Congress to assist cities is through tax policy, not through a reshuffling of Government assistance.

I would like to take this opportunity to comment on three issues, First, I would like to step back and suggest a way that Congress could use the marketplace to reshape the way it assists cities. Second, I would like to share a few of the ways that the Federal Government disrupts the functioning of the marketplace in some of my city's most troubled neighborhoods, and suggest some market-based reforms of HUD. Finally, I would like to offer a few specific thoughts on the HUD reinvention plan, which has some strong merits.

An Overview: Tax Policy as the Best Way to Help Cities

I would gladly trade all assistance from HUD—indeed, from all major urban programs—for a small Federal tax advantage for residents of large cities and a slightly larger advantage for residents of the most distressed neighborhoods. Such a tax advantage would do more to overcome 30 years of failed Federal programs and policy than any amount of Government re-engineering. My city would be able to address its own problems in its own way, within its own resources.

As the well respected business journal of my city recently editorialized,

> [A Federal tax break for residents of cities] is an idea that could reduce the cost of assisting cities by reducing the Federal bureaucracy, while at the same time giving businesses and families incentives to return to the cities' core. More people and more commerce would mean more tax revenue, thus offsetting the lost grant money. And, perhaps more importantly, such boosts in population and activity could help stem suburban flight and the risk that cities become cores of poverty ringed by affluent suburbs. It would mean restoring the financial health of cities.

Such a tax advantage would have five distinct benefits:

First, it would directly address the fundamental problem facing our cities, which is the flight of wealth. A tax incentive would apply a tourniquet to the flow of businesses and jobs out of cities.

Second, it would distribute Federal assistance to cities much more efficiently. A tax advantage instead of a series of grant programs would eliminate layers of Federal, State, and local overhead. You could clear out entire Federal office buildings and take dramatic action to reduce the size of the Federal Government.

Third, a tax advantage would reduce some of the absurd regulation with which local governments now grapple. Later in my testimony I will describe some of the ridiculous end products of well-intentioned Federal regulation in the area of housing policy.

Fourth, a tax advantage would target aid better. In the current system, Federal assistance too often goes to the cities with the most clever grant writers, not the cities with the most pressing need. Similarly, Federal assistance drives local strategies, instead of vice versa, as cities tailor their solutions and even their view of the problems to maximize their ability to obtain Federal grants.

Fifth and finally, a tax advantage would cause private dollars to do some of the investment and revitalization currently being done with Government money.

Using the Marketplace to Reform HUD

Even if Congress decides not to pursue the idea of a tax advantage for cities, there are several attractive possibilities for reforming HUD that use the marketplace and achieve some of the same goals.

HUD today provides a stark example of good people working in bad systems. Despite high-level commitment to cities and an openness to new ideas, Housing officials cannot circumvent Congressional micromanagement fast enough to help us. Common sense takes a back seat to counterproductive rules.

A few examples might illustrate the artificial world the Federal Government has created:

PUBLIC HOUSING

The Indianapolis public housing authority operates the only significant elderly high-rise apartment complexes in my city, virtually all of which are what some euphemistic developer has labeled "efficiencies." These units are 30 percent vacant because poor people, just like middle-class people, don't want to live in dense, cramped conditions. This situation contributed to our "troubled" status prior to our successful removal from that list last year. HUD rules severely limit conversion without a one for one replacement, and of course we can't, nor do we want to, build more units. If we did build more units, without full availability of a Federal subsidy we would operate the new units at a deficit, and since operating dollars are being reduced we would simply aggravate the problem.

HOME

Indianapolis is involved in a massive urban rebuilding program. As part of that project, we wanted to provide incentives to families in poorer neighborhoods to fix up their homes. I asked that HOME dollars be made available in a pilot project to work with 100 owners in a neighborhood to cause investment in literally every house. City staff rejected the idea, saying it was more practical to do 30 houses using only local dollars. Why? Because if we were to use HOME dollars, then older houses would need to be brought up to existing code, which of course no one can afford to do. Federal policy encourages decay, except by those few homeowners who can afford the high standard and who probably don't need the subsidy in the first place.

COMMUNITY DEVELOPMENT BLOCK GRANTS (CDBG)

Of all assistance programs, CDBG provides the most flexibility. We send virtually all of our CDBG funds through neighborhood-based groups, leveraging quite substantive results and investments. As part of our revitalization program, I targeted abandoned retail corners, which years ago were centers of neighborhood activity. I intended to offer matching dollars to owners or tenants willing to fix up and occupy these facades using neighborhood youth in both the construction and the retail. Of course this idea failed, since CDBG requires Davis-Bacon, which meant that the minimum wage we intended to pay young men with limited skills became impossible.

HUD AS SLUMLORD

No matter how well-intended, housing simply cannot be delivered at the national level. Too many local idiosyncrasies prevail. HUD has become a slow-moving landlord, weighted down by Congressional restrictions that virtually require it to be cumbersome.

Indianapolis had a scattered site slum project that had been built with HUD assistance. It had been foreclosed by HUD. There were no potential purchasers. It was having a very negative effect on the neighborhood.

We went to HUD and asked for a very simple solution. We would demolish the units, give vouchers to the tenants, build lower density housing on those lots and on additional lots (donated by the city) and offer units to the tenants who were displaced.

The HUD officials agreed that this plan made sense. It took more than 2 years for the City and HUD to find a way through all the obstacles contained in the law. It took 2 years to get to an outcome that everyone involved wanted to achieve. I can't imagine what would happen in a case where the parties did not fully agree.

Congress can begin to reverse the strange outcomes of failed policies of the past, but radical reform around market principles is needed.

Slashing expenditures without accompanying change is the worst of all possible worlds. Federal restrictions increase the cost of shelter and distort the marketplace in virtually every area. The following formula would provide more value for the dollar and serve as a first step toward the elimination of HUD:

1. Add all the money now spent on affordable housing and community economic development and the salaries of all the people involved in administering it, except for a small audit group. Repeal virtually every law and regulation and block grant the dollars to cities. Let those closest to the neighborhoods determine the rules.

2. Repeal the current Public Housing Program, and deed all existing buildings to the community or the local agency. Provide sufficient family-based vouchers for all the current tenants. These vouchers need to be based on the fair market rents for the community. Eliminate the one-for-one replacement rule.

Having taken this action, we will be forced to compete in the marketplace. In my case, we would demolish some units' rehabilitate some units, restructure some units, and sell some units. The result would be much improved housing opportunity for our lowest income citizens. Freed of HUD restrictions, I would be enthused by the opportunity to make the most of the housing I had inherited.

Reinventing HUD: A Blueprint for Action

Secretary Cisneros is to be commended for his hard work during his term of service. In every dealing I have had with him or his senior staff, I have found a willingness to help, an openness to new ideas, and a commitment to cities. However, in far too many instances he and they were unable to approve effective, common sense solutions because of the myriad rules and restrictions. I am pleased to see that the Secretary did not respond to the systemic problems of the HUD laws with a band-aid. He has presented a sensible, far-reaching proposal.

PRINCIPLES OF REFORM

The proposal is based upon seven principles. These principles, for the most part, read like a Mayor's wish list. They call for empowerment of local government to respond to the tremendous challenges facing cities. However, the list of principles weakens as one progresses down the list. I am concerned about the implementation of the phrase "obliged to meet certain responsibilities in return for Federal assistance." I do not question the need to confirm to Federal guidelines, I reject more specifically defined "responsibilities."

Similarly, the principles provide very specific language expressing the expectation of Federal "requirements" for fair housing and for the creation of mixed-income neighborhoods. While I do not argue with the concept, I fear the rules that will be drafted to meet that goal.

PROGRAM CONSOLIDATION

I applaud the move. It is important to clear the books of failed and unfunded programs.

COMMUNITY OPPORTUNITY FUND

For me, this is among the most positive aspects of the proposal. It recognizes that the CDBG program has helped us meet the needs of low-income neighborhoods and the people who live in those neighborhoods. The proposal combines CDBG with a number of programs that were, to be candid, unknown to me. This is a very positive move.

I worry about the accompanying regulations. The rhetoric is very good. But, if the history of the CDBG program is a guide, then there is likely to be a strong desire within HUD and those who influence HUD to limit flexibility and add new requirements. The program began in 1974 under the direction of a former Indianapolis deputy mayor. There was great initial flexibility and few unworkable rules, but by the end of the Carter Administration a regulatory morass threatened to make the program unworkable. My good friend Dick Lugar then became Chairman of the Housing Subcommittee and there was substantial return to the flexibility of earlier years. Then over the next decade there has been a constant addition of more difficult planning and compliance rules, set asides, limitations on economic development, and so on.

The proposal makes no mention of a change in the distribution formula. If HUD does not propose a change, the Committee should seriously consider a thorough examination of the formula. The formula was developed in 1974 and changed in 1977. While the formula offers a fairly good distribution compared to need, it is far from perfect. The country has changed dramatically since 1977 and the formula should be re-examined in light of the changes.

For instance, the formula uses "pre-1940 housing" as an indicator of substandard housing. The existence of old housing is not, in itself an indicator of need. For instance, in Washington, the neighborhoods of Georgetown, Woodley Park, and Cleveland Park have substantial inventories of pre-1940's housing that sell for tremendous prices. In Indianapolis, where there was a fairly large stock of frame pre-1940 housing (which was and is in poor condition) the inventory is shrinking because it

falls down. Unlike cities with brick housing stock, frame homes that are not maintained are lost.

There are a number of other, similar anomalies in the formula. Moreover, the needs of western and southern cities are not reflected in the formula. The definition of "need" is a complex issue which must be adjusted to meet the conditions of the various regions of the country. The current formula defies need for a northeastern perspective.

AFFORDABLE HOUSING FUND

This new grant program is far better than the collection of programs it replaces. While Indianapolis has done fairly well in competing for funds under the existing programs, I applaud the new approach.

However, I done understand why a separate grant program is created for the housing programs. It appears that majority of the programs being added to the AHF could be included in the COF.

Few would argue that housing and neighborhoods are not closely linked. I see no rational for the creation of a second program. I recommend a careful review to see whether most or not all of the elements of the AHF can be included in the COF.

I question the retention of the Sec. 202 program (elderly housing) as a freestanding program. Similarly, the Sec. 811 program (disabled housing) seems to be questionable as a freestanding program. These programs seem to be throwbacks to the failed project based subsidy system. If we have the funds to meet the needs of people in need, we will respond to the full range of people in need in our communities.

I also question the nonprofit set aside. It is an unneeded restriction. In my community, we will far exceed the threshold test, but we should not be required to do so. Nonprofits have enjoyed strong relationships with their communities. It is not necessary to regulate the use of one tool in the fight against poverty and urban decay in contrast to the other available tools.

I do applaud the retention of HUD ends for research and evaluation. I especially applaud the creation of a national data base of indicators and statistics. Measurement of effectiveness should be based upon outcomes. If we are effective, then there should be improvement in the statistics that measure substandard housing, neighborhood decline and other problems.

I also applaud the retention of HUD efforts to identify and publicize successful projects. As we emphasize decentralized models of problem solving, information sharing becomes increasingly important.

HOMELESS ASSISTANT FUND

There was little justification for the hodgepodge of programs created to respond to homeless problems. However, I see no reason why this population should be singled out for a special program. It appears that the Secretary and much of Congress has recognized the need to allow communities to respond to their problems in a localized manner. The needs of the homeless are just a subset of the problems of poverty. Just as Congress is eliminating the scores of welfare programs that attempt to create rifle shot solutions to specific problems, the Housing Committees should avoid the temptation to create programs for each specific poverty related problem.

HOUSING CERTIFICATE FUND

The Housing Certificate Fund is a sensible, responsible change to a program that has worked but has become cumbersome to use. I applaud the Secretary.

However, in this context, I must say that I am extremely concerned at the recent action of the House Appropriations Committee. As you know, we saw the worst possible scenario created. In the midst of supportive talk of the need to devolve power and authority to the States and the cities, the Committee cuts funding for the public housing, eliminates funding for new Section 8 vouchers, but does nothing to relieve the regulatory burden on any of the programs which we operate. We are left with little money and no flexibility. This is not an action consistent with responsible government.

PUBLIC HOUSING

I understand the Secretary's intention in creating the phased down public housing proposal. There are many PHA's that are not prepared to respond to the challenges of the marketplace.

But, the phase-in will leave thousands of families forced to live in substandard housing that is under siege by drug dealers and criminals. We need to release these families from bondage. If the Committee believes that it must phase out traditional public housing, then create an option that allows the cities that are ready to end this failed concept move forward.

FEDERAL HOUSING ADMINISTRATION

I do not have enough experience with the FHA programs to offer much advice. However, I think that FHA needs to be pruned back. FHA has succeeded in creating one of the most dynamic home ownership environments in the world. It has succeeded and now needs to be scaled back so that it does not compete with the private sector. Private Mortgage Insurance, the secondary markets and the finance industry of the Nation has replicated and improved upon the good work that FHA did. Now is the time to eliminate the staff and the cost of this unneeded program.

Conclusion

I certainly support the general direction of the Secretary's proposal. Moreover, in many of the specifics, to the extent that they are known, I support the proposal. I would urge Congress to move faster and further toward market-based reforms, but I see that where we differ, the Secretary struggled with the competing goals of the need for change with the provision of adequate time for transition by the many institutions which have built programs and businesses around the existing and long-standing programs.

Congress has a terrific opportunity to reform HUD and to develop a positive agenda for America's cities that reverses 30 years of failed Federal policy while at the same time reducing the size of the Federal Government. I look forward to working with you in this endeavor.

Thank you.

PREPARED STATEMENT OF BRET SCHUNDLER

MAYOR, JERSEY CITY, NJ

MARCH 29, 1995

Thank you for inviting me to testify today.

There is broad consensus among Republicans and Democrats alike at the Federal, State, and local level that the general approach of our current Federal social welfare programs does not work.

Accordingly, I want to commend the Clinton Administration, under the leadership of Secretary Cisneros, for beginning a serious review of the United States Department of Housing and Urban Development (HUD).

I also want to acknowledge that the incremental reforms suggested by Secretary Cisneros are a step in the right direction.

But I want to encourage all of you to be even bolder in your thinking about social welfare reform.

Most of the testimony today will deal discretely with the issue of housing, as if that need exists in a vacuum. Much discussion will focus on how HUD could more efficiently provide for the housing needs of the poor. But a more enlightened approach to social welfare would focus upon the boarder needs of the whole person.

For instance, I suspect that most of you on this Joint Subcommittee not only feel good about the fact that you can choose where you want to live, but also that you are paying your rent or mortgage with money that you have earned—not with a Government housing voucher.

Having the Government voucherize housing assistance is better than having the Government build housing projects that ghettoize the poor. But more fully reforming our welfare and tax policies, so that every American can feel the satisfaction of actually having earned the cost of their housing, and can feel, therefore, whole—just as you feel whole—is what we should be striving toward.

To this end, several mayors from across the United States including the mayors of Charlotte (NC), Dallas, Indianapolis, Milwaukee, and Raleigh (NC)—have been working together with me to fashion a document that we are thinking about calling "A Contract With America's Cities." This document will contain some of the HUD-specific recommendations that I will close my comments with today. But its centerpiece is this simple proposal: That we combine a move from welfare to workfare, with Congressman Dick Armey's Flat Tax proposal and a set of non-means-tested, refundable, earned-income tax credits earmarked for housing, food, health care, and day care.

Under this proposal, all Federal welfare programs providing federally, financed, but locally administered, workfare programs. These workfare jobs would not necessarily be publicly administered. They could be federally funded jobs with private sector firms, competitively contracted at the local level, to provide various supplementary public services. Under this system, welfare would end for all able-bodied

persons who refused to work. But for those who were willing to work (which, in my experience, is the vast majority of our welfare population), a paycheck would replace today's welfare check, and would be supplemented by the aforementioned non-means-tested, refundable, earned-income tax credits for housing, food, health care, and day care.

Combining a flat tax rate with refundable, earned-income tax credits would, even without means testing, produce significantly progressive effective tax rates.

Making these tax credits refundable—as is the case with today's earned-income tax credit program—would ensure that all Americans would equally benefit by this system, including very low-income working Americans, who, because of their low tax liability, would never be able to fully utilize simple tax credits.

Attaching these tax credits to earned income would specifically increase the rewards for work. (The Government should not be subsidizing those who refuse to work, or those who do not need to work.)

Making these tax credits non-means-tested would correct the perverse incentives of the current tax code, which reward Americans for staying poor, and which harshly penalize them if they work hard to climb out of poverty, or if they form a family and thereby increase household income.

Targeting these tax credits to the essentials or food, housing, health care, and day care would satisfy the Government's interest in making these essentials more affordable, while at the same time allowing for the elimination or other tax and income benefits. For example, deductions for mortgage interest and employer health care contributions could be eliminated, as could most other federally administered food, housing, health care and day care assistance programs.

These welfare and tax code changes would require less bureaucracy, and would cost less to administer, than our current social welfare programs. They would also ensure that no one would have an incentive to stay with a workfare job if they could find a better, private sector alternative—since, again, these benefits would not be means-tested. Yet, for the first time, every American who was willing to work would be able to obtain a job—whether private sector or workfare related—that together with their earned-income tax credits, would guarantee them the ability to earn the income they need to provide for their family.

This is really the plan that I and several other mayors would like to recommend to you as the way to fully over-haul the Federal Government's approach to providing social welfare assistance. And I hope that when I conclude my prepared remarks momentarily, you will ask me some questions about this grander plan. But if you want to focus more narrowly on small steps to reinvent HUD, let me turn at this point to some specific recommendations.

As I, and the other mayors with whom I have been working, see it, HUD currently has three major missions. Its first mission involves the distribution of urban development grant monies. We would like to see these programs consolidated into a single urban aid block grant that would be awarded by a fixed formula directly to America's cities. We want this block grant to leave our cities maximum flexibility on how that money should be spent to improve the quality of life in our urban communities, and we want to see the administrative savings generated by this streamlining of the HUD bureaucracy shared with us, because America's cities are in desperate need of new and recurring revenue sources.

The second major mission of HUD as it is currently operated is to facilitate the construction and management of public housing complexes. Rather than continue this practice, we believe that the ownership of existing public housing projects should be transferred either to their tenants, or to the cities, or to not-for profit organizations or other private entities.

In most cities, the housing problem for low-income families is one of affordability, not availability, and maintaining public housing has proven to be far more expensive than providing low-income families with housing certificates. I am the mayor of a city that has a fairly well-run Housing Authority. But it remains the case that its infrastructure is aging, and the cost of maintaining and modernizing its buildings is rising. Accordingly, it would be wise for the Federal Government not to add to this problem by constructing new, large public housing complexes.

Instead, low-income families should be given housing vouchers, as Secretary Cisneros suggests, or, more ideally, a refundable, earned-income tax income credit as part of the grander plan that I outlined for you earlier. This approach to making housing affordable would be far preferable to the status quo not only because it would eliminate Federal bureaucracy, but also, as I am sure many have already testified, because it would give low-income families the power to choose where they want to live.

HUD's "Reinvention Blueprint" calls for a dramatic expansion of the use of housing vouchers, but it also calls for the Federal Government to continue making sig-

nificant capital investments in public housing complexes. If HUD is willing to spend this kind of money, then to ensure that it is only a one-time transitional expense, the release of such investment funds should be made contingent upon a transfer of the housing project either to local governmental, or private, hands.

The third major mission of HUD is mortgage finance, principally through the Federal Housing Administration (FHA). If the FHA is to assist in the Federal Government's efforts to revitalize our cities, however, it should refocus in efforts on providing home ownership opportunities to the low-income end of the mortgage market. This has not been the way HUD has been operating, and change is long past due.

In closing, let me add a final thought. The 104th Congress has a unique opportunity to dramatically change Federal housing and urban development policies in ways that can truly make a difference in the streets of Jersey City and every major city in America. As the mayor of a poor urban community, I hope you will seize this opportunity and totally reconstruct our Federal social welfare polices based upon the principles of de-regulation, de-bureaucratization, market competition, citizen empowerment, and choice that serve as the cornerstones of the policy recommendations that I have made today. If you follow these principles, I am convinced that—without spending more money—the Federal Government will be able to improve the lives of its most needful citizens.

Again, thank you for the opportunity to share these thoughts.

PREPARED STATEMENT OF DENNIS W. ARCHER

MAYOR, DETROIT, MI

MARCH 29, 1995

Mr. Chairman and Members of the Subcommittee: I am Dennis W. Archer, Mayor of Detroit. I very much appreciate your soliciting the recommendations of local elected and appointed officials with respect to reauthorization of the Nation's housing and community development programs, including the Clinton Administration's plans for consolidating various programs of the Department of Housing and Urban Development ("HUD"), entitled "Blueprint for Reinvention."

I am here today to articulate the critical importance of a continued Federal commitment, in partnership with cities and counties. This will help promote neighborhood revitalization and expand the supply of affordable housing in our Nation's central cities, suburban counties, small towns and rural areas.

Mr. Chairman, it is important that while we talk of consolidating HUD programs, that we do not cut the funding of the department. The recently passed House rescissions bill and the impending Senate bill do this by cutting public housing development, public housing modernization, incremental rental assistance, and other important HUD programs. Cities still have overwhelming needs. Whatever shape the debate takes here in Washington, DC will not alter the fact that housing and community development needs of the citizens across the Nation will have to be addressed.

As mayors, we know that there is still a great deal to be done. The U.S. Conference of Mayors most recent *Status Report on Hunger and Homelessness in America's Cities,* a 30-city survey, makes the extent of the need very clear. The report found that last year's applicants for assisted housing waited an average of 21 months for public housing; the wait for Section 8 housing was 36 months and for vouchers it is 35 months. Sixty-three percent of the cities have stopped accepting applications for assisted housing programs due to the excessive length of the waiting list. With such conditions as these, I urge both Subcommittees to support, at the very least, the FY 1995 funding level for HUD's public housing programs.

HUD was started during the era of social cataclysm that brought us the Civil Rights Act and the Voting Rights Act. HUD has made homeowners of many of our citizens who otherwise would not know the stability, security and pride of knowing, "This is my house."

If we eliminate HUD, where will these people live? Most cities, like Detroit, have been suffering from an ever-decreasing tax base. Since 1950, Detroit has experienced a population loss of nearly 800,000 people. In the 4 years from 1988 to 1992, the Detroit Metropolitan Statistical Area (MSA) lost 39,206 manufacturing jobs and 8,398 construction jobs. The impact of this job and population loss on the tax base and economy of Detroit has been devastating. Detroit has been left with a disproportionate number of poor and limited income people. Will the suburbs absorb them? Will they live in rural areas?

Detroit's public housing system, although improving, is a troubled one. Public housing is still home to 4,570 families, of which 1,715 are senior families. If we do not house these families, who will?

I agree with many of you on a central point: We do not need a 1980's version of HUD, rife with corruption and scandal. I am of a new generation of Mayors in the United States. My generation of Mayors will not stand for the slightest hint of corruption or public disservice.

Secretary Henry Cisneros has taken the initiative to restructure and reinvent HUD. This reinvention, which you have before you today, will make HUD more efficient in delivering services to our Nation's citizens. It will also provide for the programs under HUD's scope of responsibilities to be objectively analyzed. No one is in favor of inefficient, wasteful programs or outdated policies. HUD's reinvention, as offered in this Blueprint, would bring forth this very achievement. Secretary Cisneros has taken an aggressive step and has performed tremendous, necessary surgery on HUD. Any analysis to reinvesting HUD needs this precise and delicate surgery, not a blunt, meat-axe approach.

The reinvention of HUD would call for a new accountability of HUD's programs. HUD will ask the simple questions of its programs. For example, how many people are homeowners now who were not homeowners before? Have we improved on lowering the delinquency rate on the payment of rent owed to HUD? Have we provided more low-cost housing to citizens? Programs must be able to stand on their own merit. Also, communities will be awarded for high levels of achievement.

The reinvention of HUD means that the city of Detroit will have to consider three performance-based funds instead of 60, and will no longer have to spend unnecessary time applying for multiple grants, filling out paperwork, and attempting to plan around several sources of Federal funds. Detroit can concentrate on solving the problems of housing, not red tape.

The reinvention of HUD means that nonprofit and community-based organizations would determine what is best for the citizens of our cities: Not a Federal bureaucracy in Washington, DC.

The reinvention of HUD means that more people will be able to afford their own homes through its Government-owned insurance company combined with public and private sector partners. HUD will simplify the process for many of our working poor to buy a home. HUD remains committed to the important role of the Federal Government in buying a home.

The reinvention of HUD is a reinvention not just of the mechanism of an agency, but of the attitude of an agency. HUD will become "user friendly" and address the most important need of our Nation—the housing needs of our citizens.

The poor and low-income citizens of Detroit and our Nation who need public housing had to suffer through 12 years of inefficiency at HUD. Our Nation witnessed, from 1980 until 1992, a marked decline in home ownership. This rate finally began to rise in 1993, but we are still far short of where we could be. The fact is, most people want to own a home. However, the number of citizens who pay more than half of their income on rent is rising. The number of homeless people is increasing. The House has considered, and the Senate will soon consider, legislation that would "take back" or "rescind" FY 1995 funds. These rescissions would make what once existed of the housing safety net a worthless relic.

Let me put it in plain English: These rescissions will decimate housing for the citizens of Detroit and most of our Nation's cities. Thousands of hard-working, wage-earning taxpayers who cannot afford housing without Government assistance would not have a place to live. In Detroit, for example, we want to start the demolition of unsafe and abandoned property so that Detroit can make these sites economically viable. In Detroit, we want to start creative and innovative home ownership programs to transform Parkside Homes. I cannot, and I believe most of our Nation's Mayors cannot, make life better for the citizens of our cities' confined by the shackle of these rescissions.

The feasibility of the private sector of Detroit being able to create over a thousand units of affordable, decent housing is pure folly. For many of our Nation's poor, low income, disabled, or persons afflicted with AIDS, the only housing option is HUD. As legislators and prudent public servants, in this era of scarce economic resources, your only option is an efficient HUD. As an elected official who sees everyday the impact of outdated, inefficient public housing policy, my only option is an efficient, flexible HUD.

HUD represents a real investment in our cities and our citizens. In the current fiscal year, HUD is providing $24 million in operating grants and $32 million in comprehensive grants to help provide public housing in Detroit. In addition, HUD has awarded $187 million in special grants this year to assist Detroit in bringing the quality of public housing in Detroit up to basic standards. These funds are des-

perately needed to provide poor and low-income people in Detroit with basic housing. The elimination of HUD and these grant programs would send the message to our citizens that "we just don't care." I am here today on behalf of those homeless, poor, low income, and persons with AIDS for whom HUD has made a difference. Also, I am here today on behalf of all of those Mayors who have to see and live with the pain of a growing homeless population. Finally, I am here as a person who is concerned with the growing insensitivity toward the poor.

Allow me to talk about the priority programs of local governments—CDBG and HOME.

Celebrating its 21st year having been signed into law by President Gerald Ford in 1974, the CDBG is the Federal Government's most successful domestic program. The CDBG program's success stems from its utility, i.e. providing cities and counties with an annual, predictable level of funding which can be sued with maximum flexibility to address their unique neighborhood revitalization needs. According to HUD, more than 90 percent of total expenditures are for activities benefiting low- and moderate-income citizens and their neighborhoods. HUD's most recent statistics (1990) indicated that 40 percent of that year's funds supported housing activities, 21 percent went to public works activities, 11 percent to economic development, 9 percent to public services, and the balance to acquisition and clearance of land and blighted structures, and program planning and administration.

But don't take my word as to the program's impact. A recently completed, 2-year study of the CDBG program by the Urban Institute concludes that in its 20 years' existence the program has brought "important contribution(s) to city community development, including demonstrated successes in achieving local neighborhood stabilization and revitalization objectives." The Urban Institute believes that in virtually every city, neighborhoods would have been affected detrimentally had CDBG not been implemented. The Institute claims that "the CDBG program works most effectively when communities practiced concentrated investments, linked housing, economic development and social service spending, and invited citizen participation in neighborhood planning efforts." This strategy of comprehensive treatment of neighborhoods will be greatly facilitated by the Administration's new Consolidated Plan requirements. The study also found that CDBG programs clearly benefit those for whom the program was intended—low- and moderate-income persons and neighborhoods—and does so to a substantially greater extent that the minimum (70 percent) required by law. The Urban Institute correctly characterized the program as the Federal Government's primary means to support local efforts in the stabilization and restoration of deteriorated neighborhoods.

Like CDBG, the HOME program is producing very positive results in expanding the supply of affordable housing. Enacted as the centerpiece of the 1990 National Affordable Housing Act and signed into law by President Bush, the program was initially mired by many legislative provisions which thwarted its effective implementation. After a series of legislative changes designed to facilitate effective implementation, and a firm commitment by Secretary Cisneros to make it work, the program really took off in January, 1993.

Since then the progress in using the funds, and the uses to which they are being put, is most impressive. According to HUD, as of the end of February, 1994, 99.1, 75.6, and 28.8 percent of the $3.66 billion appropriated by FY 1992, 1993, and 1994 respectively has been committed to projects, and 69.9, 31.6, and 5.5 percent has been disbursed, respectively for each of those years. This translates into 49,659 completed projects containing over 106,955 affordable housing units. Fifty-nine percent of the funds support rental housing, the bulk of which has been rehabilitated, as the statute directs. Twenty-three percent of the funds support homeowner rehabilitation, while 18 percent of that amount supports first-time homebuyers through acquisition or new construction. Three percent of the funds are being used for tenant-based rental assistance. For every HOME dollar, an additional $1.61 in non-HOME funds is leveraged. It is clear that HOME is meeting the Congressional intent of expanding the supply of affordable housing with an overwhelming majority of the funds spent on rehabilitation and new construction.

HOME funds are also deeply targeted, well below the maximum of 60 percent of area median income for rental housing and 80 percent of area median for ownership housing required by the statute. Fully 86 percent of the rental units assisted with HOME fund's go to those with household incomes below 50 percent of median. Of that, nearly 53 percent are assisting those with incomes below 30 percent of median. In many areas 30 percent of median income is actually below the poverty line. On the home ownership side, 57 percent of the funds used for those activities benefit those at or below 50 percent of median income, 16 percent benefit those between 50 and 60 percent of median income, and nearly 27 percent benefit those between 60 and 80 percent median income.

The Administration has proposed a sweeping reorganization of HUD and its programs. Some 60 individual programs are proposed to be consolidated into three block grants. Two of the consolidations—the Community Development Block Grant Fund and the Affordable Housing Fund—are proposed for FY 1996, while the Housing Certificates for Families and Individuals Fund is proposed for FY 1998. I support the Administration's proposal for program consolidation into the Community Development Block Grant and Affordable Housing Funds. I agree with the details. I am particularly pleased that the administration has selected the CDBG and HOME programs to be core elements for two of the consolidations. In addition, I will insist that in these and any other block grant programs, that the vast majority of the funds go directly by formula to cities and urban counties. I look forward to working with the Subcommittee in refining these proposals.

Mr. Chairman, I as a local government official believe strongly that there needs to be a continued and strong Federal role in housing and community development programs. Since the Housing Act of 1937, Congress has enunciated, and repeated in subsequent housing. acts, that, as a matter of national policy, the Federal Government has an obligation to assist States and local government in providing decent, safe, and sanitary housing for lower-income households. Perhaps Congress said it best in a "Declaration of National Housing Policy" including in Section 2 of the Housing Act of 1949:

> The Congress hereby declares that the general welfare and security of the Nation, and the health and living standards of its people, require housing production and related community development sufficient to remedy the serious housing shortage, the elimination of substandard and other inadequate housing through the clearance of slums and blighted areas, and the realization as soon as feasible, of the goal of a decent home and suitable living environment for every American family. . . ."

I submit to you that, while progress has been made toward this goal, it has not been fully achieved. The Federal Government must make a commitment to this national housing policy, backed up by the resources with to continue the battle against neighborhood deterioration and a decaying housing stock.

There have been questions raised recently as to whether there is a need for HUD as an agency to exist. I feel strongly that HUD needs to continue as a cabinet level agency. Mr. Chairman, I look forward to working with you and the Subcommittee in revising, reauthorizing and adequately funding HUD's housing and community development programs.

HUD Reinvention:
From Blueprint to Action

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

THE WHITE HOUSE

WASHINGTON

March 15, 1995

Dear Friends:

The Federal Government has a vital role to play in housing and community development and job growth. Economically distressed communities across our Nation need Federal help to ensure that all Americans can find decent, affordable housing in safe, clean neighborhoods.

In December, Secretary Cisneros and I proposed dramatic changes to transform the U.S. Department of Housing and Urban Development into a stronger partner of the American people and the communities in which they live. These changes, which were outlined in HUD's reinvention blueprint, will make HUD a vigorous supporter of local initiatives for empowerment. They will eliminate scores of separate and often overlapping programs, slash red tape, better use Federal resources flowing into our Nation's communities for housing development and job creation, and give local communities greater command of their own destinies.

Our earlier blueprint provided a road map for sweeping change at HUD. This document provides specific direction for turning our proposals into action. It contains hard answers to critical questions about how our proposals for change will affect our communities and our people, and it offers specific recommendations for writing these changes into legislation.

Communities throughout America need Federal resources -- which they can match with their own public and private resources -- to spur community development and job growth. These specifications for legislation are the starting point for a good-faith, bipartisan effort to ensure that our communities get the resources they need. It is my hope that this proposal will be received in the spirit in which it is offered, and that we can go forward together to help our communities build a bright future for all Americans.

Sincerely,

Bill Clinton

HUD Reinvention:
From Blueprint to Action

March 1995

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I. Introduction: An Historic Moment for America's Communities

We stand today at an historic moment for America's cities and communities and their relationship with the National government. In the wake of last November's mid-term elections, the most fundamental questions are being asked about the proper role of the National government and the extent of our national commitment to our cities and our responsibility to poor people.

- How much should we, as a Nation, do to repair the fabric of our urban centers, and especially of the communities and neighborhoods that have been left behind by the changes in our economy?
- How much responsibility should we, as a Nation, accept for housing the millions of poor and low-income working families who live in these places?
- How large a role should the Federal Government play—in comparison with cities and States—in dealing with these problems?
- What is the fundamental purpose of government in confronting these issues?

Many longstanding assumptions about the relationships among Federal, State, and local governments—and between the public and private sectors at all levels of governance—are being challenged. This debate is healthy. The minds of many are open to new ideas, to new possibilities. And we have an opportunity to make a clean break from policies and programs that have failed us, and to pursue new approaches to old problems that have long beset our urban communities.

But this moment, so rich in opportunity, is also full of peril. There is danger that in our eagerness to rectify the mistakes of the past, we will ignore the constructive lessons for the future. There is grave danger that in our haste to do *something* dramatic, we will do something destructive.

At this moment, America stands poised between acting on a new understanding of our national responsibility to our urban centers, or rejecting our responsibility altogether. We stand poised between renewal or rejection of a national commitment to help millions of people who struggle daily against tremendous odds to feed, clothe, and shelter themselves and their children.

II. HUD's Mission Is Important to America

HUD was created to carry out the Nation's commitment to work for healthy growth in cities, adequate housing for all, and protection of society's most vulnerable people.

A. Cities at a Crossroads

The United States is largely defined and given much of its character by its great cities. This Nation is known for, and draws its strength from, the great universities of Boston, the pace-setting architecture of Chicago, the creative energies of Los Angeles, and the financial power of New York City. The country is also defined — and scarred — by high crime, the high costs of illegal immigration and the fiscal crisis in many of our major urban centers. As the 21st century approaches, a great Nation needs its cities to be once again engines of economic growth and social vitality.

Fast-moving, powerful forces worldwide have disrupted long-established patterns of economic activity and social organization in every country, including the United States. Global competition and technological innovation are restructuring the U.S. economy; pressures on families and communities have generated fears for the future of young people and the Nation. Many people have been left behind, many others worry about their jobs. President Clinton has defined the challenge we face today — to embrace change by offering people and communities the opportunities they need to benefit from new sources of prosperity.

Nowhere is this challenge more urgent than in America's cities. Poor, mostly minority people have become concentrated in inner-city neighborhoods where job opportunities are virtually nonexistent, two-parent families are rare, welfare dependency is widespread, and drugs, crime, and violence are rampant. Stark differences exist between the social conditions in distressed neighborhoods and the conditions in more affluent areas. In 1990, 11 percent of the population of the 100 largest cities lived in extreme poverty neighborhoods, compared with 5 percent in 1970. Within these communities, prospects are bleak:

- More than 40 percent of working-age males, ages 16 to 64 were unemployed in the previous year, compared with just over 19 percent in non-poverty neighborhoods.

- **While 11 percent of all central city households received public assistance, 33 percent of households in extreme poverty neighborhoods were on welfare**

- **Good-paying jobs for those with less than a college education are vanishing in central cities** Between 1970 and 1990, for example, manufacturing employment just about held steady in the United States overall, while declining by nearly 11 percent in America's urban centers, including declines of 72 percent and 50 percent, respectively, in New York and Boston

Neighborhood decline tends to spread as the crime and blight of distressed communities causes residents and businesses in adjacent areas to flee. Further, the social welfare and other costs of large poverty populations cause fiscal stress that, in turn, leads to higher taxes, reduced services, and reduced maintenance of public infrastructure, driving residents and firms to seek suburban locations. In a growing number of metropolitan areas, neighborhood decline has spread from the central city to older inner-ring communities, as the pattern of decline and outward migration continues to extend the urban fringe

Despite their many problems, however, cities still serve as the foundations of vast and powerful metropolitan regions that, by 1990, were home to more than 77 percent of Americans and more than 83 percent of the country's jobs. Central cities are the leaders of these economic regions. They contain more than 30 percent of the Nation's people and more than 40 percent of its jobs. Because of the inextricable links between central cities and suburban labor, housing, and goods markets, economically healthy cities drive economically healthy metropolitan areas that are the building blocks of national economic growth

In short, the overall economic performance of metropolitan regions is linked to the performance of their central cities, with recent evidence suggesting that cities and their suburbs tend to rise—or fall—together

A Case for Private Sector Investment in America's Inner Cities

Despite their many problems, inner-city neighborhoods offer several potential comparative advantages to firms who locate there

- **Physical Location.** Inner-city areas are generally located near downtown areas and their attendant business, transportation, and communication nodes. Inner-city locations offer potential advantages for businesses requiring proximity to downtown business districts, infrastructure, entertainment and tourist destinations, and concentrations of other companies. This also creates opportunities for locating non-headquarters activities such as warehousing and data processing that benefit from proximity

- **Demand Conditions.** Inner cities represent an immense, growing, yet underserved market. Despite low incomes, inner cities have higher income per square mile than suburbs due to higher population density. Furthermore, they present opportunities for developing specialized products and services for urban minority markets

- **Linkages to Regional Clusters.** Inner-city locations offer prime access to competitive regional clusters. These local clusters represent large and often rapidly growing markets for supplies, components, and support services. Firms based in the inner city should be able to take advantage of proximity to develop close customer relationships with downtown firms

- **Human Resources.** Inner cities contain large labor pools which may possess specialized skills, a population with a strong entrepreneurial spirit that in the past has been more devoted to community service organizations than business, and a growing cadre of minority executives trained at the Nation's great business schools and with experience in large corporations who could provide leadership for inner city businesses

Source: Michael E. Porter, "The Competitive Advantage of the Inner City," in forthcoming Harvard Business Review

If the wealth of the Nation depends on the health of its metropolitan regions, then this country must strive to ensure the health of these regions. This requires converting the potential comparative advantage of cities into actual advantage in regional and global economies. The private sector must assume its rightful role as the driver of economic growth. But, the Federal Government's role is to remove impediments and increase vital public investment. Indeed, a principal challenge of national policy, and therefore of HUD, is to encourage the private sector to reinvest in America's inner cities.

The revitalization of our cities requires more than attention to bricks and mortar. This is why HUD's central mission is defined as *helping people create communities of opportunity*. The generation of new economic activity in distressed communities, and connecting inner-city residents to economic opportunities in the larger metropolitan economy are, therefore, essential elements of HUD's mission.

B. The Nation's Housing Sector: A Foundation for Families and the Economy

Every person needs a place to live, and people with troubles must solve the problem of where to live before they can make much progress on the other challenges they face. When nightfall comes or exhaustion sets in, every American must have a place to lay his or her head and a place to eat, to refresh, to store possessions.

For most Americans, housing is the single costliest expense in a household's budget. Vast numbers of households cannot afford decent housing. Between 1989 and 1993, the number of very low-income renters with acute housing needs—those paying more than 50 percent of income for rent or living in severely substandard housing — rose by 700,000, from 4.9 million to 5.6 million. And, this figure does *not* include those actually homeless. Families with children are the fastest growing population facing acute housing problems.

Homelessness is the most severe manifestation of our Nation's housing problems. The homeless population is now estimated at 600,000 on any given night. An estimated 7 million persons have been homeless at least once over the past 5 years. The causes of homelessness are complex and multi-faceted, relating to both economic distress and social ills including mental illness, substance abuse, and other chronic health problems.

Even for those who escape the worst conditions of acute housing need, dreams of homeownership are too often out of reach for moderate-income Americans. Homeownership produces essential individual and societal benefits:

- *Homeownership provides personal financial security.* Through homeownership, a family acquires a place to live and raise children and invests in an asset that can grow in value and provide the capital needed to start a small business, finance college tuition, and generate financial security for retirement.

- *Homeownership strengthens families and good citizenship:* Homeowners often feel a sense of physical and psychological security that renters do not, thus creating a more nurturing environment for families.

- *Homeownership fosters communities:* Homeownership helps stabilize neighborhoods and strengthen communities. It provides residents incentives to maintain and improve both private property and public spaces.

- *Homeownership stimulates economic growth.* Homeownership helps generate jobs because housing is a major component of the American economy. It accounts for 5 percent of the Gross Domestic Product (GDP) and nearly one-third of gross private domestic investment. Moreover, housing has always been a major force in pulling the economy out of recessions. Designing, building, and rehabilitating homes employ local labor and use a vast array of American-made products and services. Every 100,000 new units of housing creates 170,000 jobs, 40 percent of which are on-site and another 20 percent of which are in trade, transportation, and services that come primarily from local markets.

Owning a home serves as one of the main symbols of economic and social success, and is a primary aspiration for most Americans. Recent surveys indicate that 86 percent of all adults prefer to own a home, and two-thirds of all renters would buy a home if they could afford one.

Recent trends in homeownership have not been encouraging. From the end of World War II to 1980, homeownership rates rose steadily, peaking at 65.6 percent in 1980. After 1980, the overall ownership rate declined. The rate began rising once again in 1993, but the current homeownership rate is still well below its historic peak.

HOMEOWNERSHIP RATES
(Percent of all households)

	1983	1993
Overall	64.6%	64.0%*
White Households	67.7	67.4
Black Households	45.0	42.5
Hispanic Households	43.0	41.2
All Households (25-29)	38.3	33.6
All Households (30-34)	55.4	50.8
All Households (35-44)	69.3	65.1

*Revised downward from 64.5 percent based on adjusted 1990 Census weights rather than 1980 Census weights.

Source: Bureau of the Census, Department of Commerce

Although homeownership rates for higher income households headed by persons over 45 years of age have held steady, those for younger households and those with lower incomes have not. Ownership rates for households headed by persons under the age of 35 and for low- and moderate-income families fell significantly during the 1980s. Most disturbing is the decline in the rate among very low-income families with children: 37 percent of these families owned their own homes in 1979, but only 29 percent did so in 1989.

In addition, homeownership rates are substantially lower among members of minority groups than for whites. In 1993, 43 percent of all black and 40 percent of all Hispanic households were homeowners, compared with 70 percent of all white non-Hispanic households. This inequity holds across income levels: higher income and lower income minorities alike are less likely to own their own homes than are their white counterparts.

From homelessness to homeownership, HUD has a mandate to address national housing concerns. But many are now calling for the dismantling of HUD, arguing that housing interests would be better served if the Department's programs were scattered among other Federal agencies. There are compelling reasons why the American people have supported a cabinet-level agency whose primary focus is housing and communities.

First, despite housing's central role in individual, family, and community life, the cost of housing is often beyond the financial reach of ordinary people. Consequently, millions of households cannot afford decent-quality housing without government assistance. Therefore, to the extent that the Federal Government has a goal of ensuring that all families live in decent, affordable housing, there is a need for a housing agency. This is why every industrialized nation in the Western world has a national agency whose mandate is to increase the supply and quality of affordable housing.

Second, the extent of housing needs varies substantially across States, cities, suburbs, and rural communities. So do housing costs, and the local commitment and resources to address them. Because the housing problems of the vast majority of the most vulnerable citizens and working families are income-related, they are most appropriately addressed through policies at the Federal level. The Federal Government cannot effectively devolve this responsibility to States and localities.

Third, beginning with the Homestead Act more than a century ago, and augmented in 1913 by Federal tax incentives, the Federal Government has fostered and supported the ideal of homeownership. The promotion of homeownership opportunities for all Americans — but particularly working families, members of minority groups, and residents in underserved areas — also demands the undivided attention of an agency whose principal business is housing.

Finally, only the Federal Government can oversee the work of eliminating discrimination from our housing markets. Housing discrimination and segregation undermine the health and vitality of our Nation's communities. Discrimination denies minority families full and free choice about where to live, while denying minority neighborhoods the services and resources they need to thrive and grow.

America's bedrock values include fairness and equality of opportunity. The basic American formula is work today and sacrifice now for tomorrow's gains. Nothing is guaranteed, but the equation generally works. There are, however, some Americans for whom the rules do not work. They have a job, they have saved money, they have a clean credit report. But they can't get a housing loan because of the neighborhood they live in, or because of the color of their skin, their gender, or their family composition. Such discrimination is not only against the law, but it is also devastating to our hopes for building a society with true justice for all.

Thus, the idea of fairness is a unifying theme for HUD's work. Nothing else can work if the essential ingredient of fairness is not there.

C. HUD Serves Poor and Vulnerable Populations

Decent housing gives families and individuals dignity, self-respect, and the platform they must have to meet their other needs. This is especially true for the Nation's least fortunate populations, including the homeless, the frail elderly, disabled people, and those suffering from the ravages of HIV/AIDS. The private market alone will not meet the basic housing needs of these vulnerable populations because that housing must be linked to specialized services. Service providers despair of effectively serving these groups when their housing is unsuitable, when they are constantly evicted because they cannot afford the cost of decent housing, and when, all too often, they become literally homeless.

Many in society have grown weary of confronting homeless people on our Nation's streets. But that weariness does not make the scourge of homelessness disappear. The homeless are with us and must receive our compassion and our assistance to put roofs over their heads, provide access to services, and open up opportunities for self-sufficiency. The needs of the homeless are greater than charities or local governments can afford. The Federal Government must support local systems to provide a continuum of care for the homeless to offer them a way off the streets and into society's mainstream.

It is particularly tragic when children become homeless. Families with children are a growing fraction of the homeless and a growing fraction of those whose acute housing needs make them vulnerable to becoming homeless. Without an address from which they can attend school, a kitchen table at which to do homework, a stable community of neighbors, or a parent who has access to training and jobs, how can children thrive and grow up to be responsible, contributing, caring adults? Families with children need affordable housing in safe, nurturing communities. It is particularly important for families with children to have access to homeownership when that is their aspiration.

One-third of the 3.6 million very low-income elderly households have acute housing needs and no housing assistance. Most of this population are paying more than half their meager incomes for housing. Housing programs successfully serve the elderly, enabling many to stay home, giving others the ability to move into an elder community where their increasing physical and other needs are met in a way that gives them dignity and preserves their independence. The private market is creating new ways of meeting the housing needs of an aging population, but it will not serve those who are alone and poor as well as old.

Disabled people have a whole spectrum of housing needs, depending on the type and extent of their disability; lack of suitable housing poses a special threat to their well-being. People with chronic mental illness and limited financial resources end up on the streets or in hospital emergency rooms if they do not have a stable address that provides the right level of on-site supervision by their mental health caseworker. The quality of life for the developmentally disabled similarly depends on good housing with the right level of supervision and links to supported work and other sources of self-esteem.

HUD has helped create a variety of flexible, community-based housing solutions with special design features for those with special needs over the past two decades: group homes, transitional housing, single-room occupancy (SRO) facilities, and independent apartments linked to supportive services. These unique housing resources can neither be sustained nor meet additional needs without Federal resources. And the additional needs are considerable. Nearly half of all very low-income disabled individuals have acute housing needs measured *only* as severe rent burden or inadequate housing, not even taking into account needs for service-linked housing.

Persons with HIV/AIDS face unique challenges. Their increased health care costs combined with loss of income make them especially likely to become homeless because they can no longer pay the rent where they presently live, while property owners are afraid to rent to them. For persons with HIV/AIDS, adequate housing can prolong life. These same individuals would have a life expectancy of 6 months on the streets.

Housing is the nexus for other government agencies to address the needs of the homeless, the disabled, frail elderly people and persons with HIV/AIDS. Without housing, the social safety net becomes nothing more than a jumble of loose threads. Many people in these populations depend on Federal resources to keep a roof over their heads, as well as to support their most basic tasks of daily living. For some, the existence of a Federal agency to help them meet their basic housing needs is the difference between life and death. HUD is their lifeline.

III. HUD: Changing With the Times

HUD and its predecessors have an impressive record of accomplishment

- Since its foundation in 1934, the Federal Housing Administration (FHA), a vital part of HUD, has insured new mortgages and refinanced home loans for 23 million families, including 1.3 million in 1994 alone. Millions of families have become homeowners for the first time because the Federal Government has stood with them at a time when they needed a financial partner.

- More than 7 million families have lived in public housing supported by HUD subsidies. Despite its troubling image today, public housing has historically been a starting place for a better life. Congressman Louis Stokes of Cleveland and Congressman Joe Moakley of Boston, Bill Cosby, Kenny Rogers, Whoopie Goldberg, Isaiah Thomas, Aaron Neville, Evander Holyfield, Vernon Jordan, Juan Williams, Bob Georgine, Diana Ross — all of these distinguished Americans got their start in public housing.

- Nearly 12.5 million families and individuals — including millions of senior citizens and people with disabilities — have found affordable housing in privately owned, federally assisted rental developments. They were able to move from back rooms to independent living because HUD was there to help.

Hundreds of communities, thousands of neighborhoods, and tens of millions of people have benefited from HUD programs over the past three decades. The national commitment that was renewed and strengthened when HUD was established in 1965 has been honored in communities from border to border and coast to coast.

At the same time, HUD must acknowledge its failures. This means abandoning failed housing and community development policies that have contributed to the current crisis by concentrating very low-income families in dense, high-rise public housing projects, and by discouraging poor people from seeking work. It means ending policies that see subsidized housing as a destination rather than a new start in life, and policies that support projects over people and buildings over neighborhoods. It means doing away with centralized, overly bureaucratic, top-down approaches that tell communities what they need and how to go about solving their problems. It means reversing the historical practice of creating a separate program for every problem and a new regulation for every situation. And it means finding new ways of relating to cities and metropolitan regions, community-based organizations, and the private sector.

Principles of HUD's Reinvention

HUD shares the public perceptions of what's wrong with the old Federal program approach. In accordance with President Clinton's government-wide National Performance Review, HUD launched an effort to reshape itself for the future. The principles of HUD's reinvention are:

- Low- and moderate-income families should have greater power to make decisions about their lives, and government should support their quest for self-sufficiency;

- Decisionmakers at the neighborhood, local, and State levels should have maximum flexibility to design and utilize Federal resources, consistent with national objectives;

- Representatives of the community must have input on decisions through a comprehensive consolidated planning process;

- Recipients of Federal resources, whether individuals, localities, or States, should be obliged to meet certain responsibilities in return for the Federal assistance;

- HUD resources should be used to end the physical and social isolation of low-income populations by encouraging linkages between distressed communities and regional housing and labor markets; and

- The Federal Government has an essential and appropriate role in upholding national ideals that may be difficult to sustain locally, especially with regard to fair housing goals.

These principles provide the foundation for HUD's reinvention. The reinvention plan has three components.

1. Consolidate Programs Dramatically

HUD's reinvention will radically overhaul the current system and transform the Federal relationship with America's communities. HUD proposes to consolidate 60 major HUD programs into three performance-based funds—a Community Opportunity Fund, an Affordable Housing Fund, and Housing Certificates for Families and Individuals.

The three performance-based funds will have the following characteristics:

The **Community Opportunity Fund (COF)** will stimulate community revitalization. All current HUD grant programs for community development—including Community Development Block Grants (CDBG) and Economic Development Initiative grants—will be consolidated into this fund. Localities and States will have broad flexibility to use resources to stimulate business growth and expand job opportunities in distressed communities and connect residents to job opportunities in the larger regional economy

The **Affordable Housing Fund (AHF)** will support production and rehabilitation of affordable housing. All current HUD grant programs for development of housing for low- and moderate-income households will be rolled into this fund, which will be administered by local and State governments.

The **Housing Certificates Fund** will provide direct assistance to low-income households for affordable rental housing and for homeownership. All current public housing, assisted housing, and Section 8 rental assistance programs will be combined into this certificate fund, which will be administered by local public housing agencies (PHAs). Program reforms will maximize metropolitan housing opportunities for residents of extreme poverty neighborhoods by eliminating administrative barriers across jurisdictional lines, prohibiting local residency requirements, and expanding resources for metropolitan area-wide landlord recruitment and tenant housing search assistance.

This consolidation will sweep away the clutter of separate application procedures, rules and regulations that has accumulated at HUD over the past 30 years, as programs were piled on top of programs. And it will free cities and States to solve their own housing and community development problems in their own ways

Important national ideals are embedded in law and in practice. Among them are: fair and open housing, serving those most in need — those in financial need as well as those with disabilities — and empowering people and communities to choose their own destiny Recipients of money from these funds will be expected to administer programs consistent with these ideals

Recipients will also have a powerful incentive to put performance ahead of process, just as HUD is doing HUD's new funds will be performance-based. That means cities and States that produce real, tangible results for the people and communities who need help today — more affordable housing, expanded homeownership, business growth, increased job opportunities—will earn bonuses of more resources and increased flexibility. Cities and States that do not perform will not receive extra funds. Those who fail to meet clear statutory objectives such as financial accountability and low-income targeting could face cuts. HUD is building serious fiscal and market discipline into these funds.

2. Transform Public Housing

HUD proposes to phase out direct public housing subsidies to PHAs. Instead of subsidizing buildings and bureaucracies, HUD will provide direct assistance to residents They will choose where they want to live. This approach will enable PHAs to compete with private landlords for subsidized and unsubsidized tenants. Tenant-based rental assistance will be governed by a pricing system that pegs assistance to the local cost of decent housing. When this transition is complete, public housing will be indistinguishable from conventional housing, from the renter's viewpoint, and it will be a true asset to communities.

Under the current system, PHAs are not subject to market disciplines. PHAs do not have the flexibility to demolish the worst housing stock, and, in fact, face perverse incentives to rehabilitate rather than replace, regardless of cost efficiencies. Even the best PHAs have been hampered by inflexible statutes and regulations, which limit innovation and decision-making based on local needs and opportunities.

To remedy the above, HUD will give PHAs more flexibility to meet local needs, while requiring effective performance, as judged by residents and the market, not just HUD. The proposal envisions three stages: deregulation and program consolidation; market-based rents with project-based assistance; and market-based rents with tenant-based assistance.

During the first transition stage, beginning in fiscal 1996, HUD will consolidate dozens of disparate public housing programs into two accounts: one for capital and management improvements and one for operations. HUD will also decontrol and deregulate the 3300 public housing agencies that are performing well. Federal micromanagement will be supplanted by local bottom-up planning and flexibility, enabling PHAs to utilize their resources to best meet local needs and opportunities.

All agencies will be given the flexibility to determine which units to modernize and which to demolish, providing incentives for quick demolition of some of the most distressed units With the worst public housing

demolished, PHAs will then have the flexibility to make the remaining public housing stock generally competitive.

HUD will turn its attention towards those 100 agencies that continue to exhibit severe management deficiencies. New, enhanced receivership powers will be sought, giving HUD the ability to intervene aggressively in these pereniall "sick" agencies.

During the second transition phase, existing capital and operating subsidies will be converted to project-based assistance. This transition will give agencies experience with operating on a market discipline, where rents rather than government-determined capital and operating budgets drive management of the property.

In the final phase, subsidies will be converted to tenant-based assistance. Tenants can choose to stay in their units or move to private rental housing.

3. Bring Homeownership Within Reach of More Americans

On November 5, 1994, President Clinton stated

> ...today I am directing HUD Secretary Cisneros to develop, in cooperation with the most significant members of the housing industry and government at all levels, a plan to boost homeownership to an all-time high in the United States...a detailed strategy that recommits America to homeownership, that will add millions of new homeowners by the end of the century.

In response, HUD established a National Homeownership Partnership, bringing together the resources and commitment of the housing industry's major public, private, and non-profit organizations. The goal of that partnership will not be achieved without substantially increasing homeownership opportunities to moderate-income families, members of minority groups, newcomers to the United States, and residents of communities who aspire to own their own homes but whose needs have not been met by the conventional mortgage market. Serving these needs is FHA's primary mission.

HUD will improve the efficiency of FHA by transforming it into a business-like, government-owned Federal Housing Corporation (FHC), which will work more effectively. Where possible, it will tap the strengths of private market partners to expand homeownership opportunities. The new corporation will continue to serve the needs of working families who require low downpayment loans, and residents in central cities, older neighborhoods, and other underserved markets. In hard times, it will maintain the flow of mortgage capital to areas suffering economic downturns. And, it will help finance more affordable rental housing.

For the past 60 years, FHA has played a critical role in all these areas, filling a niche where the private sector would not, or could not, serve. FHA is a Fortune 100-sized insurance company with a $380 billion portfolio of insurance in force backed by the American taxpayer. But it is increasingly technologically obsolete and ill-equipped to manage its business. By creating a new government-owned Federal Housing Corporation, Congress will transform today's FHA into a results-oriented, financially accountable credit-enhancement operation while ensuring its capacity to continue serving the homeownership and affordable rental needs of people and places that the private sector leaves behind.

FHA is too important a financial partner to first-time homebuyers, those with too little cash to make big down-payments and to underserved people and places to abandon. For example,

- FHA provides homebuyers with a meaningful low downpayment financing option, a necessity for many cash-strapped first-time home buyers: 87 percent of those who purchased a home with an FHA loan in 1993 made a downpayment of less than 10 percent, and 67 percent were first-time buyers. In contrast, of those who purchased a home with a conventional loan sold to Fannie Mae or Freddie Mac that year, only 20 percent had low downpayments and just 31 percent were first-time buyers.
- In 1993, almost 30 percent of FHA home purchase loans went to underserved areas (that is, low-income and high-minority census tracts), compared with only 15 percent of conforming conventional loans.

FHA also opens the door to homeownership for minority households. FHA accounted for 35 percent of all home purchase loans made to black and Hispanic homebuyers in 1993. Excluding VA and conventional loans above FHA's loan limits (so-called "jumbos"), FHA accounted for about 45 percent of all home purchase loans to black and Hispanic metropolitan homebuyers.

FHA meets the needs of borrowers who are not likely to be adequately served by private companies whose primary interest is maximizing profits. Compared with loans originated by conventional mortgagees, FHA borrowers have lower incomes, purchase lower-valued homes, make lower downpayments, are more likely to be first-time homebuyers or members of a minority group, and are more likely to live in low-income, high-minority neighborhoods. For example, in 1993 more

than 60 percent of all homebuyers with FHA loans had low downpayments, compared with virtually no mortgage loans insured by private mortgage companies.

The Result: A New Department of Housing and Urban Development

The consolidation of programs into broad and flexible funds, the devolution of programs to localities and States, and the creation of entrepreneurial government organizations will change the way HUD does business.

HUD will shift from a lumbering bureaucracy to a streamlined partner with State and local governments. Significant downsizing is anticipated, reducing HUD's current workforce of 12,000 today to fewer than 7,500 employees. The current 80 field offices will shrink to roughly 60. And a new structure will be put in place to oversee the performance partnerships. The new HUD will be capable of the following functions:

Performance Measurement and Accountability

HUD's performance partnerships will incorporate performance expectations and measures to ensure results. Performance measures will describe how States and localities use their funds and the benefits produced for people and communities.

This approach is being pioneered in Oregon, where State officials are able to negotiate with Federal agencies on how funds are used--but then must set goals and achieve results. Performance measurement in HUD programs, and especially in the proposed performance grants, will provide the flexibility that local decisionmakers need to address local problems. But it will hold these decisionmakers accountable for results.

HUD will work with Congress to design systems to reward outstanding performance. HUD will also publish rankings of performance measures for program recipients. These rankings will be used to determine where technical assistance or additional HUD oversight is needed. And, the mere existence of these rankings will create pressure locally to improve performance where it is found lacking.

Clearinghouse

No community should have to reinvent the wheel. HUD will play an important role in identifying and disseminating model housing production and community revitalization strategies that can be replicated in other jurisdictions. Information-sharing will be enhanced through conferences, demonstrations, awards for model programs and projects, and the use of modern technology.

No longer will HUD staff only be masters of the regulatory detail. Instead, HUD staff will be expert in packaging and refining successful local program models for replication in other jurisdictions.

Oversight

HUD will continue to provide oversight and enforce the law in a number of key areas, including civil rights, operation of government-sponsored enterprises, real estate settlement processes, regulation of interstate land sales, enforcement of lead-based paint standards, and manufactured housing, and ensure that Federal housing funds are used to create jobs for low-income residents.

IV. Conclusion: Bipartisan Spirit Has Fashioned HUD

Our Nation's 60 years of housing and urban development policies have been fashioned in a bipartisan spirit, with broad Congressional agreement over national goals and spirited differences over the means of achieving them.

In response to the Great Depression, President Franklin Delano Roosevelt established the Federal Housing Administration that revolutionized our Nation's system of housing financing and established a public housing program to provide housing to working people facing unemployment.

In 1946, on the eve of the elections that gave the Republican party control of Congress, Senator Robert A. Taft wrote

> I believe that the Government must see that every family has a minimum standard of decent shelter along with subsistence, medical care, and education....

Senator Taft — "Mr. Republican" — fought alongside Democrats of his day for a national commitment to decent, affordable housing, which is the bedrock of healthy communities and the foundation of economic lift for families. And the vision of Senator Taft and his bipartisan allies became a national commitment in the Housing Act that President Harry S. Truman signed into law in 1949. The 1949 Act declared:

> The general welfare and security of the Nation ... require ... the realization as soon as possible of a decent home and a suitable living environment for every American family....

President Truman, Senator Taft, and other leaders of their day looked at post-war America and saw a terrible housing shortage. They did not blame people who needed a hand up. They made a bipartisan, national commitment to help them.

In March 1965, in a message to Congress proposing the creation of HUD, President Lyndon B. Johnson said

> We want to build not just housing units, but neighborhoods; not just to construct schools, but to educate children; not just to raise income, but to create beauty and end the poisoning of our environment

And that year, 1965, with the strong support of the Congress, the U.S. Department of Housing and Urban Development was born. The Nation reaffirmed and strengthened its commitment to our communities and the people who live in them.

Less than a decade later, a Democratic Congress passed, and President Gerald R. Ford signed, the bipartisan Housing and Community Development Act of 1974. The Act consolidated a number of older categorical programs into the Community Development Block Grant program, HUD's first formula block grant designed to simplify administration of Federal assistance and increase the discretion of local officials. It also replaced several project-type housing construction programs with the Section 8 program and featured for the first time tenant-based rental assistance in the form of housing certificates designed to increase individual choice and mobility.

President Clinton and the Republican-led 104th Congress now face another critical opportunity to forge a bipartisan partnership for housing and community development policy for the 21st century. HUD's blueprint for change offers that opportunity.

Chapter One: Program Consolidation

More than any other Federal agency, the U.S. Department of Housing and Urban Development (HUD) is defined by its relationship with communities across the Nation. Everything HUD does — enhancing homeownership opportunities, providing rental assistance to low-income families, expanding the supply of affordable housing, stimulating neighborhood economic activity — is geared towards supporting the development and maintenance of healthy, thriving communities of opportunity.

HUD's relationship with communities has in recent years deteriorated substantially. As documented extensively by Congressional Committees, the HUD Inspector General, the General Accounting Office, and the National Academy of Public Administration (NAPA), HUD's effectiveness has been diminished by the proliferation of dozens of separate, duplicative programs. The statutes and rules governing these programs, in turn, are generally complex and overly prescriptive, leaving little room for innovation or flexibility either by HUD staff or by the communities they serve. These detailed requirements reflect the philosophy that the Federal Government knows best. Program implementation is further constrained by an agency "culture of micromanagement" that places principal emphasis on procedural accomplishments rather than real results.

HUD's current state impedes the ability of communities to respond to housing and community development issues in a coordinated way. By allocating funds through many separate programs and to numerous grantees in a given jurisdiction, HUD has undercut the incentive for local and State governments to engage in coordinated strategic planning. By treating target areas — affordable housing, economic opportunity, service-enriched housing for special populations — in isolation, HUD has inhibited comprehensive solutions. The result is a fragmented, balkanized delivery system that operates inefficiently and, at times, ineffectively.

HUD's current state also places intolerable administrative burdens on HUD's customers, particularly State and local governments, nonprofit organizations, private-sector entities, and resident organizations. Each program has had its own guidelines, applications, funding schedules, award criteria, and monitoring systems. For many customers, navigating through this programmatic minefield requires the expenditure of scarce organizational resources — further diminishing the funds devoted to actual affordable housing and community development.

Finally, HUD's current state has diminished the effectiveness of HUD staff. HUD has too many responsibilities and activities for an agency that is one of the smallest in the Federal Government. The nature of those responsibilities also tends to make HUD's staff passive recipients of information and applications rather than true partners for change in communities.

HUD's reinvention will radically overhaul the current system and transform the relationship of the Federal Government with America's communities. HUD proposes to consolidate 60 major HUD programs into three performance-based funds — a Community Opportunity Fund, an Affordable Housing Fund, and the Housing Certificates Fund.

The three performance-based funds will have the following characteristics:

The **Community Opportunity Fund (COF)** will stimulate community revitalization. All current HUD grant programs for community and economic development — including Community Development Block Grants (CDBG) and Economic Development Initiative grants — will be consolidated into this fund. Localities and States will have broad flexibility to use resources to stimulate business growth and expand job opportunities in distressed communities.

The **Affordable Housing Fund (AHF)** will support production and rehabilitation of affordable housing. All current HUD grant programs for development of housing for low- and moderate-income households will be rolled into this fund, which will be administered by local and State governments.

The **Housing Certificates Fund (HCF)** will provide direct assistance to low-income households for affordable rental housing and for homeownership. All current public housing, assisted housing, and Section 8 rental assistance programs will be combined into this certificate fund, which will in most instances be administered by public housing agencies.

As the attached chart indicates, the move towards program consolidation will proceed in phases. In FY 1996, HUD's major programs will be consolidated into seven performance funds. In addition to the three funds mentioned above, HUD will continue to administer during a transition period two public housing funds (one for capital, one for operating), a consolidated homeless

SUMMARY OF HUD'S PROGRAM CONSOLIDATION

Current Major Programs (60)	FY 1996	FY 1998 & Beyond
Public/Indian Housing Development	PH/IH Operating Subsidies	Housing Certificate Fund
Public/Indian Housing Amendments		
Severely Distressed Public Housing		
PH Major Reconstruction		
Public Housing Coordinators		
PH Vacancy Reduction		
Tenant Opportunity Program		
Urban Youth Corps		
PH/IH Modernization		
Family Investment Centers		
PH Youth Apprenticeship		
PH/IH Operating Subsidies	PH/IH Operating Subsidies	
Drug Elimination Grants		
Youth Sports		
PH Service Coordinators		
Section 8 Certificates	Housing Certificate Fund	
Section 8 Vouchers		
Section 8 Contract Renewals		
Section 8 Family Unification		
Section 8 for Persons w/Disabilities		
Section 8 for Persons w/AIDS		
Section 8 for Homeless		
Section 8 Opt-Outs		
Section 8 Counseling		
Section 8 Pension Fund Certificates		
Section 8 Veterans Affairs Supportive Housing		
Section 8 Headquarters Reserve		
Lease Adjustments		
Family Self-Sufficiency Coordinators		
Flexible Subsidy	FHA Multifamily Housing Resolution Activities	
Title VI Preservation Program		
Section 8 Property Disposition		
Section 8 Loan Management Set-Aside		
Elderly Housing Service Coordinators		
Project-Based Service Coordinators		
Congregate Housing Services		
CDBG	Community Opportunity Fund	Community Opportunity Fund
Economic Development Initiative		
EZs/Economic Development Initiative		
UDAG Recaptures		
Youthbuild		
Colonias		
Early Childhood Development		
Neighborhood Development		
Community Adjustment Planning		
HOME	Affordable Housing Fund	Affordable Housing Fund
National Homeownership Fund		
Housing Counseling		
Elderly Housing (S 202)		
Housing for the Disabled (S. 811)		
HOPE 2		
HOPE 3		
Lead-Based Paint Hazard Reduction		
Shelter Plus Care	Homeless Assistance Fund	
Section 8 SRO		
Emergency Shelter Grants		
Supportive Housing		
Innovative Homeless Initiative		
Rural Homeless Grant/Safe Havens		
Housing Opportunities for Persons w/AIDS	Housing Opportunities for Persons w/AIDS	

fund, and the AIDS housing program. In addition, FHA will carry out housing resolution activities for its multi-family portfolio.

The homeless fund is itself a consolidation of HUD's six separate McKinney homeless programs. Consolidation of these competitive programs into a single formula grant based on need will enable communities to develop continuum of care systems to address their homeless needs comprehensively.

An orderly and rational transition is needed for a number of reasons. Keeping homeless and AIDS programs separate is necessary to ensure the continued, discrete emphasis on service-enriched housing for vulnerable populations. The housing needs of these populations are generally served by a network of government and non-profit providers that is separate and distinct from the network of affordable housing developers. Integration of such disparate systems must proceed with care to ensure adequate treatment of these vulnerable populations. In addition, communities require time to develop and implement new continuum of care systems for the homeless before those systems are integrated into the mainstream programs.

The transformation of public and assisted housing must also be carried out prudently to prepare older properties — operated for decades without market discipline — for transition to a competitive market environment. For public housing, the decontrol of program administration, the setting of market rents, and the upgrading of the existing inventory must precede transition to the private market. Similarly, assisted housing developments will become market competitive through a Federal Housing Administration (FHA) "mark-to-market" process, along with rehabilitation where necessary to minimize costs and protect tenants. This process must be implemented before the conversion of project-based subsidies to tenant-based assistance and allocation of such assistance to public housing agencies for administration takes place.

HUD expects the bulk of the consolidation to three performance funds to be complete by FY 1998. Where necessary, public housing agencies will be given additional time to convert to tenant-based subsidies. The consolidated homeless fund will also be kept separate until FY 2000 to provide maximum protection for this vulnerable population and time to establish a coordinated system to address its special needs.

HUD's consolidation proposal goes beyond the 60 major programs considered critical to the agency's mission. HUD's Inspector General has identified up to 240 total HUD activities — a hodgepodge of active programs, inactive programs, set-asides, technical assistance funds, eligible activities, regulatory functions, and insurance authorities. HUD's reinvention plan is comprehensive and will address each activity identified by the Inspector General. Specifically, HUD's reinvention includes proposals to:

- Consolidate an additional 59 activities (mostly subsets of the major programs that have been identified) into the 3 performance funds;
- Consolidate 29 separate insurance authorities into just 2;
- Phase out 29 programs that are no longer active;
- Terminate 37 programs that are duplicative or no longer necessary; and
- Ultimately consolidate 15 technical assistance programs into a simplified support system for each of the new performance-based funds.

The appendix to this document reconciles the Inspector General's list of 240 programs with HUD's reinvention plan. The tables in the appendix demonstrate how each activity identified by the Inspector General will be treated under the reinvention plan.

HUD's reinvention plan will transform the relationships among local, State, and Federal levels of government on issues of housing and community development as part of a new performance partnership. This move to program consolidation and performance-based funding will be an act of **responsible devolution**. The plan will give localities and States the flexibility to tailor strategies to local market conditions and the resources essential to carrying out those strategies.

Through this new flexibility, localities will be able to develop comprehensive strategies that coordinate local and State approaches to homelessness, affordable housing, and community development. These community and housing investment needs, by their very nature, vary from jurisdiction to jurisdiction and change from year to year.

Through their Consolidated Plan, localities will have the flexibility to create these coordinated strategies based on local needs. The Consolidated Plan will serve as a unified application — a "one-stop-shop" — for numerous Federal programs. By using new computer and information technologies with HUD-supplied software, localities will communicate substantial amounts of information to their citizens in an understandable format. HUD-supplied advanced computer-mapping capabilities will enable citizens to understand precisely how taxpayer

The Consolidated Plan

President Clinton believes that to meet our new challenges, government must provide the tools all Americans need to reach their fullest potential. In describing his vision of a New Covenant in his 1995 State of the Union address, he stated

> Our New Covenant is a new set of understandings for how we can equip people to meet the challenges of the new economy, how we can change the way our government works to fit a different time, and above all, how we can repair the damaged bonds in our society and come together behind our common purpose.

The President's approach is to fundamentally restructure the relationships between government and the American people, restoring citizen involvement in government.

In response to the President's call for a New Covenant, HUD is establishing a new covenant with those it serves. This new covenant affirms that citizens and elected officials must work together to rebuild their own communities. It has two principal goals: to reconnect people and government and to streamline Federal and local government relations. The major instrument to facilitate and achieve these goals is the Consolidated Plan, which serves as the planning and application system through which States and localities, in partnership with their citizens, can access key HUD reinvented and consolidated programs.

The Consolidated Plan builds upon a basic democratic principle: Citizens and communities know what is best for their community. It engages citizens with their government by facilitating a dialogue on common goals and a common vision.

This new arrangement is based on "bottom-up" citizen-inspired and -initiated planning. It enables communities to engage in a more creative process and allows local officials to explain, in the citizens' own terms, how they can be helped by government programs. It recognizes that government must talk to citizens in terms of the problems and opportunities communities face every day and not in terms of individual programs. It provides localities and their citizens flexibility to plan in terms of their own local needs.

Partners: Federal and Local Governments

The Consolidated Plan dramatically transforms the role of the Federal Government. It ends the "program mentality" which relied on developing new programs for every problem instead of developing a comprehensive approach to communities and people. For too long the "program mentality" suffocated local initiative and creativity. This move calls for discarding outdated systems and implementing holistic approaches. It focuses on maximizing community resources rather than the strictures of the program rules and regulations.

Learning from the positive lessons from the Empowerment Zone program, the Consolidated Plan can serve as the key step in enabling local governments to access a myriad of federal government programs through a single one-stop-shop. As currently structured, it takes what used to be 12 separate planning, application, and reporting requirements and incorporates them into a single document for HUD's major formula community development programs. And it will serve as the basis for States and localities to access even more funds as outlined in this chapter.

From Rhetoric to Reality
The Consolidated Plan also recognizes that government must join in the technology revolution. In an age when a plastic card accesses bank funds, government should not be constrained to forms and pencils. Indeed, the potential for a technologized federal government is limitless. The information it possesses and encompasses is unequaled.

HUD is working to lead this technology revolution. Through the Consolidated Plan, HUD will communicate this information through satellite television networks, interactive cable television, telecommunications systems like the InterNet, and other advanced modalities. The audience will be State and local governments, and citizens, linked by computer for the first time in history.

The technology will follow three critical steps:

Step One: Provide Information for Strategic Planning

HUD has developed computer technology which includes information about: housing conditions, poverty conditions, unemployment, the concentration of demographic groups, the location of schools, churches, recreation centers, etc. The information is then organized and accessed by state, county, city, census tract, or even the street or block level. This information will be used by communities to develop plans and strategies for future development. For example, job creation strategies, education proposals, housing complexes, and transportation systems could be coordinated, mapped, budgeted, and communicated. HUD will have a national database to provide citizens and governments with national lessons and models.

Step Two: Facilitate Discussion and Consensus

Once an issue is identified or plans developed, HUD technology will generate and facilitate a dialogue concerning those proposals. A national electronic townhall will give all citizens the opportunity to participate in the future of their community. Communication could be from homes, libraries, universities, or community centers.

Step Three: Develop Performance Measures

As discussed in more detail in this proposal, once the plan is developed, discussed, and finalized, the government must focus on implementation and service delivery. The Consolidated Plan process will serve as the basis for developing benchmarks for effective performance and for comparing performance among jurisdictions.

dollars are being spent, without having to speak the language of Federal program technicians.

HUD's reinvention also builds on the imaginative community and housing partnerships that have formed throughout the Nation in recent years. It will leverage Federal resources by supporting alignments of State and local government, private industry, nonprofit organizations, and community-based groups. Similarly, the reinvention plan builds on the successes that local governments have already had with Federal programs that provide substantial resources through formula-based funding. Thus, the COF is modeled on the CDBG program, which has successfully combined targeting on low- and moderate-income families with substantial local flexibility. Similarly, the AHF will build on the successes of the HOME program, which has created more than 50,000 affordable housing units across the Nation, successfully targeting low-income (more than 70 percent of renters benefited by the program have incomes below 30 percent of median) and elderly (more than 20 percent of households served) people.

At the same time, greater local flexibility will be accompanied by demonstrated performance and compliance with clear conditions that promote **national ideals**. The experience with block grant programs has demonstrated that it is critical to define conditions to which all

recipients must adhere in designing and implementing their programs. To do otherwise — to allocate billions of Federal dollars "without any attached strings" as some have suggested — would be irresponsible.

HUD's reinvention plan identifies goals and objectives that deserve national attention.

- **Maximum choice and dignity for families.** HUD's reinvention recognizes that government must put people first. It underscores the dignity of families and individuals, enabling them to choose where they live. It recognizes the special needs of homeless families and children, and provides incentives to further core values which help keep families together such as homeownership and opportunities for employment. It helps citizens move from being passive recipients of aid to full participants in their community.

- **Community participation.** HUD's reinvention recognizes the key role that all elements of the community, including community-based organizations, should play in developing and implementing strategic plans. The Consolidated Plan will establish a framework for broad-based community participation, including setting performance benchmarks consistent with local needs and priorities; development of a continuum of care strategies under the consolidated homeless fund will also draw on citizens' knowledge and expertise through local advisory boards. In addition, the AHF will continue the HOME program's set-aside for community-based organizations. Finally, HUD will continue to provide operational support for community-based organizations under the AHF and the COF.

- **Expanded commitment to America's most vulnerable populations.** The three performance funds will contain income-targeting rules, similar to those under current law, to ensure that low-income Americans are the prime beneficiaries of scarce Federal resources. Locally developed preference rules under the Housing Certificate Fund will provide further targeting. In addition, the Consolidated Plan process (together with the process for establishing a continuum of care for homeless assistance) will require localities to consider the needs of special vulnerable populations, including the homeless, disabled, elderly, and people with HIV/AIDS. Eligibility for bonus funds will be based on performance, including low-income targeting.

- **Compliance with Federal fair housing laws.** As under current law, HUD's reinvention plan will require jurisdictions to administer their programs and activities in a manner that affirmatively furthers fair housing. Jurisdictions will analyze impediments to fair housing and develop plans designed to address those impediments. HUD's reinvention will streamline the regulatory process governing the development of affordable housing and end HUD's current practice of subjecting jurisdictions and developers to restrictive "site and neighborhood standards" on a case-by-case basis. These standards, intended to steer development towards non-impacted areas, have instead led to significant delays in the development process and exacerbated disinvestment in minority neighborhoods.

- **Values of work and homeownership.** HUD's reinvention recognizes that citizen empowerment carries with it key responsibilities. The consolidated performance funds will place special emphasis on job creation for low-income persons, self-sufficiency for the homeless, and special housing opportunities for the working poor, providing an extra boost for those struggling to lift themselves up. The new job creation focus of the COF makes clear the importance of jobs to make neighborhoods work. A special emphasis on homeownership — through the development of community homeownership strategies, the use of rental certificates as a stepping stone to homeownership, and the expansion of resources for first-time homebuyers — brings added focus to the key role of homeowners in revitalizing communities.

Localities and States will be held accountable for results under the new performance funds. Localities will set clear benchmarks for measuring their own progress both toward national ideals and toward addressing local needs. These benchmarks will give citizens the ability to gauge local performance; HUD will also be able to compare performance among differing jurisdictions. Rather than dictating process, HUD will look instead at objective products, such as numbers of affordable housing units created, and outcomes, such as increases in homeownership rates and access to rental housing.

The level of performance will have real consequences for recipients of Federal funds. Good performers will have access to bonuses and other benefits, while those who fail to meet clear statutory objectives will risk reduced funding and reallocation to other recipients.

In sum, HUD's reinvention plan — and particularly the move to program consolidation and performance-based funding — reflects the centrality of HUD's commitment to America's cities. Reinvention offers a new model of flexible funding resources that can be coordinated to meet local needs. It will provide an opportunity for communities to address their problems comprehensively, coordinating their approaches to homelessness, affordable

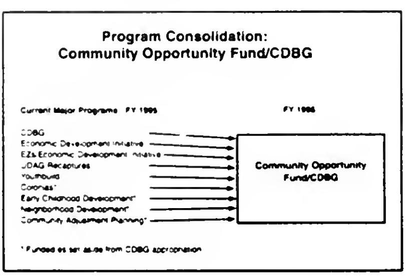
housing, and community and economic development. And it offers real opportunity for America's neediest citizens.

Through the Consolidated Plan and the program consolidations in this proposal, HUD's role will change from that of regulator to that of enabler, working with communities, citizens, local elected officials, nonprofit organizations and foundations, and private labor and industry in creating partnerships for housing and community development. HUD will both provide necessary resources and serve as a catalyst for innovation, a clearinghouse for creativity, and an advocate for America's cities and needy populations.

The following sections describe the specific funds that will serve as the basis for this new relationship between the Federal, State, and local governments. Subchapters A and B describe the two key funds that will provide resources directly to States and localities for community development and affordable housing development. Subchapters C and D describe two funds focused on the housing needs of particularly vulnerable populations, the homeless and persons with HIV/AIDS. These two funds will transition into the AHF once systems have been established to address the unique needs of these populations. Subchapter E describes the Housing Certificate Fund, which will be established to empower households through providing vouchers for tenant-based housing assistance.

A. Community Opportunity Fund

The COF reflects HUD's commitment to providing a flexible funding vehicle to communities across the Nation for community development benefiting low- and moderate-income individuals. It serves as the primary vehicle for the revitalization of our Nation's cities and neighborhoods, thereby providing opportunities for self-sufficiency to millions of Americans. This fund will consist of two related components: the CDBG program as a base and a new job creation Performance Bonus pool for good performers. A locality's Consolidated Plan will serve as the planning, application, and reporting mechanism for COF funds. Under the Consolidated Plan, the community will identify community and neighborhood development needs, actions to address those needs (including specific activities on which CDBG dollars will be spent), and the measures against which its performance will be judged. The Consolidated Plan will also provide the community a vehicle for identifying key low-income neighborhoods for targeted multiyear investment strategies.



The COF will consolidate a wide range of program activities and initiatives, including: the existing CDBG program, together with its loan guarantee (Section 108) feature; the Economic Development Initiative; Leveraged Investment for Tomorrow (LIFT); the Community Viability Fund; the Colonias Assistance program; and the array of items that are funded under the authority of Section 107 of the Housing and Community Development Act of 1974 (Special Purpose Grants).

This proposal borrows the strongest and most widely supported element from current community development programs (CDBG) and uses it as the basic structure for incorporating additional programs and instilling a strengthened job creation emphasis. Combining the existing CDBG program with a new job creation emphasis, along with a new bonus pool, has the advantage of building on what works while making the fund an even more effective tool for economic empowerment and job creation. The CDBG program already offers substantial flexibility to grantees; relatively little change is needed for that purpose. This proposal does, however, continue the current efforts to streamline CDBG by clarifying the definition of eligible activities addressing job creation and polluted or industrially contaminated urban sites ("brownfields"). Its job creation emphasis can also provide an added tool for localities' efforts to create jobs for people on welfare.

Under COF, HUD will establish national goals and objectives, while localities will determine how to achieve them. Under this new performance partnership, local performance will be geared toward achieving a series of performance measures in which the Federal Government provides the categories while the locality establishes the number to be achieved. These local performance measures will be created through the Consolidated Plan process to reflect the specific needs and priorities of particular communities.

CDBG for Job Creation:
A Source for Revitalizing Weakening Local Businesses

FLEX-TEC, INC.
Stewart County, Georgia

Flex-Tec, Inc., located in one of Georgia's poorest counties, was the recipient of a 1991 CDBG loan which assisted the company's growth and simultaneously enabled its workforce to upgrade their skills. The company, one of the area's few employers, was operating in an abandoned school building and suffering from numerous manufacturing inefficiencies. A unique combination of financing and layering of business and employee support services was used to assist the company

The Georgia Department of Community Affairs (DCA) provided a $175,000 CDBG loan to rebuild the facility. The Georgia Institute of Technology, Industrial Extension Service, coordinated the project and also provided assistance with market development and manufacturing efficiency improvements. As a prerequisite for the CDBG assistance, the company agreed to consider employer literacy training. DCA obtained the assistance of the Georgia Department of Adult and Technical Education and the local Literate Community Program, which tested the workers and designed a training program.

The company has prospered and the number of employees has grown from 30 to 66. Many of the workers are single female heads of households who have been eager to take advantage of employment and training opportunities.

Performance against these measures will determine whether the grantee qualifies to compete for a grant under the Performance Bonus pool. These goals will focus on "end-stage" outcomes, such as decreases in poverty or teen unemployment, rather than on process measurements. In addition, grantees will establish specific benchmarks as the principal means to ensure that they are progressing toward the broad statutory goals of providing decent housing, a suitable living environment, and expanding economic opportunity, principally for lower-income persons.

HUD will establish a $250 million Performance Bonus pool to reward effective performance. HUD will award bonuses on a competitive basis to fund larger-scale job creation and "brownfields" clean-up projects that are not adequately handled through the CDBG program. Awards will be based both on the merits of the specific project proposed and on the grantee's performance in the CDBG program. Projects funded will spur community economic revitalization in low-income areas, with emphasis on job creation for low-income persons. Projects will also be aimed at revitalizing neighborhoods in distressed urban areas. This federal support will help build on the many potential comparative advantages of inner-city neighborhoods, leveraging private investment and removing barriers such as brownfields that hinder revitalization.

Local Flexibility and Program Design

Under the existing CDBG program, grantees have considerable flexibility to select from a broad array of activity types, which will be retained and improved by (a) clarifying the eligibility of using funds for economic development; (b) identifying brownfields rehabilitation as a separate eligible activity; and (c) expanding the eligible activities under the Section 108 loan guarantee program to include all activities eligible under CDBG. Moreover, activities undertaken by a grantee for affirmatively furthering fair housing would not be subject to the percentage limitations on public services or planning and administration.

Under this proposal, States will gain added flexibility in how they spend their funds. States will also be allowed to carry out activities themselves in nonentitled areas. States can thus focus efforts on rural and undeveloped areas that may lack the capacity to carry out activities on their own. States could, at their option, also contract directly with other entities to carry out the needed activities, including regional planning or development bodies

CDBG funds will continue to be allocated to States and localities based on need, with the existing allocation of 70 percent of funds to entitlement cities and 30 percent to States retained.

Prior to determining these allocations, it is proposed that 0.5 percent, but no less than $23 million, be set aside for technical assistance and university programs, with up to 0.4 percent, but no less than $18 million initially, set aside for management information systems.

This will provide $10 million for community development technical assistance for localities and building the capacity (including operating and project costs) of neighborhood-based and community development organizations that wish to participate in local community development. Thirteen million dollars will be used to provide direct financing to Historically Black Colleges and Universities as well as other universities engaged in activities tied into the localities' Consolidated Plans.

The funding for developing, implementing, and refining of management information systems is critical to establishing a national database on local needs and program performance as well as to providing localities and other community members with software to plan and track performance. As the necessary systems are implemented and refined, funds needed for this purpose are anticipated to decrease over time.

Vulnerable Populations

The existing CDBG requirement that activities meet the three national objectives of benefiting low- and moderate-income persons, addressing slums and blight, and urgent need and that at least 70 percent of funds benefit low- and moderate-income persons will be retained. The current CDBG targeting practice, in which an average of 90 percent of funds benefit low- and moderate-income persons, is expected to continue.

States bordering on Mexico will continue to be required to set aside up to 10 percent of their CDBG allocations each year, as determined by the Secretary, for use in addressing needs in Colonias. In addition, a provision to allow States to contract with nongovernment entities or to carry out activities directly could be particularly beneficial in serving Colonias areas.

A 1.5 percent set-aside for federally recognized Native American Nations will be established to ensure that these needy populations are served. The Secretary will also be authorized to set aside up to 1.5 percent of technical assistance funds for assistance to Native Americans, as well as to establish out of the overall funds set aside for Native Americans a bonus pool for good performers. Under this proposal, the Insular Areas will be treated as they are under HOME, with 0.1 percent of the COF funds distributed on a formula basis.

A Successful Brownfields Re-Use Effort:
Ambridge, Pennsylvania

Beaver County, which lies northwest of Pittsburgh, saw 30,000 steelworkers lose their jobs during the 1980's. The American Bridge Division of the U.S. Steel Groups, whose 8,000 workers cut, welded, and painted the beams for the San Francisco-Oakland Bay Bridge on its hundred-acre site, shipped its last product in 1982. It was not until 1991, however, that this site — blessed with river, rail, and interstate highway access — saw renewed economic activity.

WorldClass Steel, Inc. began, in 1987, to look for a site to build a modern mini-mill. The Ambridge site was selected. Of the range of environmental clean-ups needed at the site, the worst remediation problem entailed removing about 18 inches of lead-contaminated soil. WorldClass began its steel-pickling operations in 1991. In August 1994, WorldClass announced plans for a $375 million expansion slated to produce one million tons of high-quality steel annually by the end of 1996 for the profitable automobile, consumer electronic, and housing markets. The expansion, with cleanup now underway, will provide up to 450 new jobs in the depressed Beaver Valley area.

Source. Bartsch, Charles and Elizabeth Collaton "Industrial Site Reuse, Contamination, and Urban Redevelopment: Coping with the Challenges of Brownfields." December 1994.

Performance Measures and Bonuses

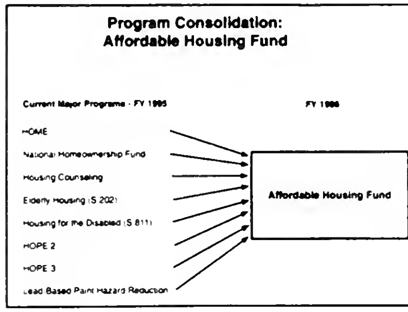
COF will institute a new series of performance measures (including separate standards for the expenditure of funds by States and localities) and establish a $250 million Performance Bonus pool. States and localities that fail to meet clear statutory objectives, including financial accountability and low-income targeting requirements, will be subject to having those funds reallocated to the bonus pool. Bonus funds will be used for specific job creation projects to revitalize low-income residential neighborhoods and to clean up brownfields. Special consideration will be given to projects that link low-income residents of distressed areas with job opportunities that enable them to enter the mainstream regional economy.

Grants under the Performance Bonus pool will be awarded on a competitive basis to grantees for specific job creation projects. In addition to the specific project proposed (including involvement of locally based nonprofits and leveraging through the Section 108 program and other private financing), other criteria for awards will include:

- The grantee's performance in expending funds in a timely manner;
- The ambitiousness of the grantee's performance levels compared with those in similarly situated jurisdictions;
- The extent of low-income targeting by the grantee, with emphasis on the creation of jobs for low-income persons; and
- The extent to which the grantee devotes and leverages its CDBG funds to job creation and to implementing neighborhood investment strategies to revitalize distressed neighborhoods.

B. Affordable Housing Fund

The Affordable Housing Fund (AHF) reflects the Federal Government's commitment to helping communities increase the supply of affordable housing, homeownership and providing rental housing for America's poor and vulnerable populations, including the elderly and disabled. A community will use its AHF funds in accordance with that locality's Consolidated Plan, which will identify housing needs, actions to address those needs (including strategies for low-income homeownership), and performance measures, all within the context of a larger plan for community revitalization. Communities can use the AHF as one prong of a coordinated approach to community development, together with the Community Opportunity Fund and the Housing Certificate Fund, to serve as tools for revitalizing communities.



Consistent with the need to provide localities flexibility in using government programs, AHF will consolidate funding for what were previously a wide range of independent programs, including the HOME Program, the Section 202 and 811 programs for the elderly and disabled, the National Homeownership Fund, Housing Counseling, HOPE Grants, and Lead-Based Paint Hazard Reduction. The six existing Stewart B. McKinney Homeless Assistance Act programs for the homeless will be consolidated into a single Homeless Assistance Fund in FY 1996, and will merge into the AHF in the year 2000, as further described in the Homeless Assistance Fund section. The Secretary will be authorized to accelerate the transition to AHF, when deemed appropriate, for communities that have succeeded in establishing a continuum of care for the homeless.

Rather than creating a new superstructure of separate programs, AHF will borrow the strongest and broadest plank from the current affordable housing production programs and place all Federal housing development funds on the same foundation supported by the Consolidated Plan. Thus, the HOME Program — which is already accessed through the Consolidated Plan by more than 500 participating jurisdictions, including States and localities — will serve as the framework around which the AHF is constructed, thereby incorporating its existing statutory protections. Using the HOME Program as the basis will permit a speedy transition as localities will not have to learn to administer a new Federal program. AHF will also build on the existing relationships among the Federal, State, and local governments, nonprofits and private industry to leverage additional resources for affordable housing.

AHF will continue the process of streamlining the current HOME Program requirements, which has already led to a dramatic increase in affordable housing production over the past 2 years. HUD will establish national goals and objectives, while localities will determine how to achieve them. Under this new performance partnership, local performance will be geared toward achieving a series of performance measures in which the Federal Government provides the categories while the locality establishes the number to be achieved. These local performance measures will be created through the Consolidated Plan process to reflect the specific needs and priorities of particular communities.

Localities will be judged by performance measures that will reflect both "end-stage" outcomes, such as increases in the homeownership rate among low-income households, and progress toward these goals. The measures will both serve as the foundation for national program performance and provide a yardstick against which local performance can be measured and rewarded through funding from a bonus pool established with 10 percent of the AHF allocation.

Local Flexibility and Program Design

Through program consolidation, AHF will replace the current mix of competitive and formula-based programs that have distributed funds in an uncoordinated fashion to a mixture of local governments, nonprofits, and other recipients. AHF grant allocations will follow the existing HOME formula, which distributes funds to States (40 percent) and localities (60 percent) on the basis of need. This approach will provide States and localities with a predictable stream of resources so that they can rationally plan and implement affordable housing initiatives, and achieve their objectives, in a comprehensive fashion.

To provide State and local governments flexibility in meeting their needs for affordable and special needs housing, AHF will permit a broad range of activities to assist rental and homeownership efforts. Essentially, all activities currently eligible under the programs being consolidated will be eligible, including rehabilitation, new construction, acquisition, tenant-based rental assistance, and first-time homeownership assistance.

In addition, this menu of expanded AHF activities will include:

- **Supportive Services** — AHF will authorize grantees to fund supportive services for the frail elderly or at-risk elderly, subject to the same conditions as the Section 202 program.
- **Service Coordinators** — AHF will cover Section 202 program costs for service coordinators, to the same extent currently allowed under 202.
- **Housing Counseling** — AHF funds will be available to provide information and counseling services to renters, to potential homebuyers before and after purchase, or to conduct housing counseling programs for the community.
- **Public Housing Modernization** — This activity will become an eligible AHF expenditure once the transition of public housing to tenant-based assistance is complete.
- **Project-Based Rental Assistance and Operating Subsidies** — The Section 202 and 811 programs as currently structured rely on project-based rental assistance. The Department has found that the use of such assistance is particularly helpful in the development of housing that serves populations with special needs. AHF will retain the current general language of the HOME statute permitting project-based rental assistance.

Up to 10 percent of AHF grants will be available for administrative costs, and up to 5 percent for operating expenses for community-based private nonprofit organizations. Neighborhood deconcentration efforts and local flexibility will be enhanced by permitting fair housing activities as an eligible use outside of the cap on administrative costs.

Localities will also be permitted to provide AHF funding to PHAs for any eligible use, should the locality choose to do so under its Consolidated Plan. As part of this coordination, localities will in their Consolidated Plan examine needs for public housing demolition and disposition, as well as outline plans for assisting troubled PHAs.

To add flexibility and increase homeownership opportunities, AHF will establish a loan guarantee program similar to the Section 108 authority for the CDBG program. This authority will give jurisdictions an additional source of financing for large-scale housing and homeownership tract development. This financing will be secured by the jurisdiction's current and future AHF funds and other security. Under this proposal, the Department will finance the required credit subsidy budget authority from the total amount requested in the Department's FY 1996 budget.

To assist in implementing the AHF, 2.5 percent of AHF funds (but no less than $83 million) will be set aside for technical assistance and community viability. This

provision reflects the need for added technical assistance for a substantially expanded base of nonprofit housing providers, specifically elderly and disabled housing providers, fair housing agencies, and housing counseling agencies. It also reflects the need to provide technical assistance for migrant farmworker housing assistance and capacity-building (including operating and project costs) of community-based organizations generally, including neighborhood-based nonprofit affiliates of religious organizations. Work-study and university community outreach will receive $10 million of these funds

In addition, up to 0.5 percent, but no less than $16.5 million initially, of AHF funds will be set aside for management information systems. This set-aside is critical to establishing a national database on local needs and program performance as well as to providing localities and other community members with software to plan and track performance. As systems are implemented and the need for refinements is identified, funds needed for this purpose are anticipated to decrease over time.

Protecting Vulnerable Populations

The existing programs proposed for consolidation into AHF are designed to benefit differing income levels and populations including the disabled and the elderly. For example, the Section 202 and 811 programs must benefit persons below 50 percent of median income, while the National Homeownership Trust assists families with up to 115 percent of median income in high-cost areas.

To ensure that the needs of vulnerable populations are adequately addressed with federal resources, AHF will generally maintain the existing limitations in the HOME program on rents and income targeting. Thus, the existing HOME requirement that funds be used to benefit families with incomes below 80 percent of area median income will be applied across all the funds consolidated into AHF. In addition, AHF will adopt the requirement for rental housing that 90 percent of the families have incomes below 60 percent of median and 20 percent of the units in projects be occupied by families below 50 percent of median income. To stimulate neighborhood revitalization and reduction of low-income concentration, localities will be authorized to use a limited portion of AHF funds for families with up to 115 percent of median income in designated low-income areas, such as qualified census tracts for purposes of the Federal low-income housing tax credit

Special efforts will also be made to ensure that needs of some of the most vulnerable populations are addressed For example:

- 1.5 percent of the AHF allocation will be set aside for Native American Nations, of which the Secretary could hold back 10 percent consistent with the performance measure provisions of AHF. This provision will increase housing production funding for Native Americans from $14 million under HOME in FY 1995, to approximately $50 million under AHF in FY 1996. This money will be distributed on a formula basis, but the Secretary will be authorized to fund smaller Native American communities, which would otherwise receive de minimis annual funding, on a different basis. Only federally recognized Native American Nations will be eligible. The Secretary will also be authorized to set aside up to 1.5 percent of technical assistance funds for Native Americans.
- The current HOME statutory treatment for Insular Areas will also be retained in the AHF.

Affordable Housing Fund:
Building on the Success of HOME

The City of Pinole, in Contra Costa County, California, held a Grand Opening for Pinole Grove Senior Housing on October 20, 1994. Pinole Grove Senior Housing is a 70-unit apartment building with a multi-use community center for low- and very low-income seniors.

The well-designed Pinole Grove Senior Housing was made possible through a successful public-private partnership led by BRIDGE Housing Corporation, an experienced regional nonprofit developer. In addition to HOME and CDBG funds, financing sources for the Pinole Grove development included Low Income Housing Tax Credits and commitments from the Pinole Redevelopment Agency, the National Consumer Cooperative Bank, Sanwa Bank, Savings Association Mortage Corporation, and Mission Housing Investment.

- In addition to the above set-asides, which occur prior to the allocation to State and local jurisdictions, the four border States of Texas, New Mexico, Arizona, and California will be required to set aside up to 10 percent (as determined by the Secretary) of their State allocations for addressing the needs of Colonias.

- Furthermore, States and localities with significant migrant farmworker populations will be required to identify the housing and other needs of these populations in their Consolidated Plans and to set aside funding to address these needs.

Nonprofit Set-Aside

To retain and strengthen the delivery infrastructure, AHF will establish a set-aside of 30 percent for all types of nonprofits, including traditional sponsors of elderly and disabled housing, to carry out eligible AHF activities. PHAs will also be eligible to receive funding from localities under this set-aside. One-half of this amount, or 15 percent of each jurisdiction's allocation, must be applied to community-based private nonprofit organizations.

Finally, the new 30/15 standard will be a benchmark, rather than a rigid requirement. Thus, if a jurisdiction presents convincing arguments why it cannot reach these specific allocations in a particular year (e.g., lack of nonprofit capacity), it will be able to vary from the benchmark.

Performance Measures and Bonuses

AHF will institute a new series of performance measures, including standards for the expenditure of funds, and establish a bonus pool. These measures will include items such as addressing the needs of vulnerable populations (including the elderly and disabled), expanding homeownership, and increasing access to affordable housing through items such as construction of rental units and rehabilitation, etc. Given broad national objectives, localities will determine the specific measures needed to meet local needs, the time frame for doing so, and a plan for achieving these benchmarks. Ten percent of the overall AHF allocation will be used to create a bonus pool for excellent performance. States and localities that fail to meet clear statutory objectives, including financial accountability and low-income targeting, will be subject to having funds reallocated to the bonus pool.

The performance bonus pool will be available to jurisdictions that surpass key Federal objectives such as percent of funds expended, low-income targeting, leveraging, and creating low-income homeownership opportunities.

Childhood Lead Poisoning Prevention

The problem of childhood lead poisoning remains important as we move to create a leaner and more efficient agency. HUD will continue the lead-based paint agenda in three primary ways. First, HUD will consolidate the LBP grant program into the new performance-based AHF. To ensure State and local responsibility for lead testing, hazard reduction, and abatement, HUD will design performance measures and incentives or "bonuses" in AHF for lead activities.

Second, HUD will continue the regulatory oversight of lead-based paint requirements in housing policy. HUD will continue to ensure that rehabilitation of all pre-1978 housing provided by the three proposed performance-based funds meets the lead requirements set forth in Title X of the Housing and Community Development Act of 1992.

Third, HUD will provide $10 million in technical assistance to State and local governments to support lead research, technical studies, and education materials. These funds will be provided in addition to the technical assistance set-aside described above. For instance, HUD will continue to:

- Fund the National Lead Information Center's hotline and clearinghouse, which provides toll-free information in both English and Spanish to the general public and professionals (from health care workers to general contractors);

- Evaluate the cost and effectiveness of alternative ways of reducing lead-based paint hazards;

- Prepare technical guidelines on safe, effective, and affordable ways to test for and abate lead hazards in housing;

- Evaluate the accuracy of devices used to test for lead in applied paint;

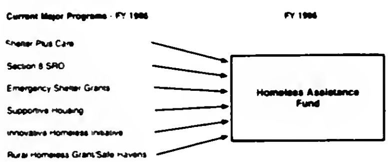
- Develop consensus standards for testing and abating lead-based paint hazards; and

- Assess the levels of public awareness of lead-based paint hazards and work in coordination with other federal agencies to develop targeted public education campaigns.

C. Homeless Assistance Fund

Reducing homelessness is HUD's number one priority. If we are to move from the current crisis of homelessness, community-based, comprehensive efforts are necessary. This proposal will consolidate HUD's six McKinney homeless programs into a single Homeless Assistance Fund (HAF) to enable localities to shape a comprehensive, flexible, coordinated "continuum of care" approach to solving, rather than institutionalizing, homelessness. Ultimately, the HAF will be consolidated into the AHF by the year 2000.

Program Consolidation:
Commitment to Special Needs Population
Homeless Assistance Fund



Homelessness is not caused merely by a lack of shelter, but involves a variety of underlying, unmet needs — physical, economic, and social. Dealing effectively with the problems of homelessness requires a comprehensive system of housing and necessary services for each stage — from emergency shelter, to transitional housing, to permanent housing with supportive services as needed, together with a strong prevention strategy. Under the continuum of care approach, communities can develop seamless homeless systems to assist individuals and families in achieving independent living.

The proposal will restructure the way the Federal Government assists one of our Nation's most vulnerable populations. It will enable localities to establish a system that can address the needs of different homeless populations while providing a coordinated continuum of care that ensures the support necessary to help those who are homeless attain permanent housing and move toward self-sufficiency. It will replace the existing maze of separate programs with a single needs-based formula grant to States and localities. It will require broad participation by not-for-profit providers and others, both in developing and implementing continuum of care plans.

The Consolidated Plan will serve as the basis for the HAF application, identifying needs and inventory, assessing the needs of homeless citizens, and linking efforts to address homelessness together with other housing and community development resources. In addition, for a community to receive HAF funds, a local board — including homeless providers (representing a broad range of subpopulations), advocates, representatives of the business community, and homeless persons themselves — will develop a more detailed plan describing the comprehensive homeless assistance system to be created to fill gaps between the identified needs and inventory described in the Consolidated Plan. This document will specify the facilities, permanent housing, and services to be created and by whom, and will establish benchmarks for measuring performance. The community will have maximum flexibility to shape solutions, but will be held to high performance standards as a condition of funding.

Consolidation and Flexibility

This proposal will consolidate the Emergency Shelter Grants (ESG), Supportive Housing, Shelter Plus Care, Section 8 Moderate Rehabilitation (SRO), Safe Havens/ Rural Assistance, and the Innovative Homeless Initiatives Demonstration Program into a single performance fund (HAF), distributed to States and localities through a needs-based formula.

This consolidated fund will address several key problems that plague community efforts to address homelessness. The McKinney grant programs currently require providers of housing and services to apply to discrete funding categories for particular needs. Each categorical program has its own funding cycle — application process, set of rules, criteria, and reporting requirements — which increases processing time and paperwork and hampers project development and implementation.

In addition, as a result of current funding mechanisms, communities and providers often have been compelled to design programs to meet funding requirements rather than actual needs. This has hampered efforts to coordinate community-based efforts to address and prevent homelessness, and isolated communities' approaches to homelessness from local housing and social service systems. The new fund will enable communities to design continuum of care approaches that reflect local conditions and opportunities, ensuring that each of the elements of the continuum of care system are in balance.

Under this proposal, funds will be provided to localities through a formula that will generally follow the current ESG formula, except that 75 percent of the funds will be allocated to cities and counties and 25 percent will be reserved for States for use in areas outside of cities and counties receiving direct formula allocations. A "hold-harmless" provision will ensure that communities that received ESG in 1993 and onward will continue to qualify for direct formula allocations. In addition, formula allocation communities will receive at least the average amount they received from HUD's McKinney programs each year between 1987 and 1993. This will provide localities with the flexibility to establish continuum of care strategies and with the resources to help implement those strategies. The Secretary will allocate 1.5 percent and 0.20 percent for Native American Nations and Insular Areas, respectively, while $25 million will be available for technical assistance. Ten percent of total funding will be used to create a bonus pool for good performance.

States and localities will also enjoy significant flexibility both in eligible uses of the fund and in administering the fund. HAF will incorporate and extend flexibility to all eligible activities currently authorized under the existing McKinney homeless programs. Localities can choose from a broad menu of activities and exercise the flexibility to select those that best address local circumstances. Specifically, recipients will be authorized to carry out activities to benefit homeless individuals and families (e.g., acquisition, rehabilitation, new construction, operations, real property leasing, tenant assistance, project-based rental assistance, supportive services, administration, and capacity building) in support of the following types of projects

- **Emergency Assistance** — Preventing homelessness or meeting the emergency needs of homeless individuals and families including prevention, outreach and assessment, and emergency shelter.

- **Safe Haven Housing** — Providing housing and low-demand services and referrals for homeless persons with serious mental illness who have been unwilling or unable to participate in mental health or substance abuse treatment programs or to receive supportive services.

- **Transitional Housing** — Providing housing and appropriate supportive services that are designed to facilitate the movement of homeless persons to permanent housing.

- **Permanent Supportive Housing for Persons with Disabilities** — Providing community-based housing and supportive services for homeless persons with disabilities, either as part of larger projects or in facilities designed solely for persons with disabilities; and appropriate permanent housing options for all homeless families and individuals.

- **Single Room Occupancy Housing** — Providing a single unit (which need not include a kitchen or bathroom) for occupancy by one person, which may include services such as mental health services, substance abuse treatment, job training, and employment programs.

Recipients could also undertake other projects determined by the Secretary to further the purposes of the HAF.

States and localities will also have significant flexibility in administering the fund, as they could choose either to administer the fund directly or to designate a public agency or nonprofit organization or consortium to administer it. States will be able to choose to administer grant amounts themselves or have the Secretary administer their grant amounts on a competitive basis to areas of the State outside cities and counties receiving formula distributions. These non-formula allocated localities will also have the flexibility to administer their funds on their own, or to have the funds administered through a designated public agency, private nonprofit organization, or the State.

States will have the option of using up to 15 percent of their formula allocations to carry out their own homeless assistance programs, with the remaining 85 percent distributed to nonformula-allocated localities.

Community Participation

To facilitate comprehensive, effective, and coordinated approaches to homelessness, the proposal will require broad community participation in the development and implementation of the homeless strategy:

- Each recipient will be required to establish and support a local board to assist the recipient in developing the application, determining how the program will be administered, overseeing the activities carried out under the program, and evaluating the recipient's performance in carrying out these activities. States will establish and support a State advisory board with similar responsibilities.

- Each recipient will be required to make available at least 51 percent of its annual grant to private nonprofit organizations for providing assistance to homeless individuals and families.

- The Secretary will be required to establish additional appropriate citizen participation requirements to ensure that all needs of the homeless and homeless subpopulations are taken into consideration.

Comprehensive Approaches and Performance

The local and State advisory boards will prepare, for inclusion in recipients' applications, a detailed description of a comprehensive homeless assistance system designed to fill gaps in homeless assistance identified in the jurisdiction's Consolidated Plan. This continuum of care plan will provide clear benchmarks for judging the recipient's performance.

The continuum of care plan will establish a system of outreach and assessment; provide for emergency shelters and transitional housing with appropriate supportive services and for permanent housing or permanent supportive housing; coordinate funds received under HAF with other Federal, State, and local programs available to assist homeless individuals and families; and develop a system of referrals for subpopulations of the homeless (including homeless veterans) to the appropriate agencies, programs, or services necessary to meet their needs.

Applications will also include a multiyear strategy for establishing and maintaining this continuum of care, including timetables and budget estimates, together with a 1-year action plan, a description of efforts to address the problems faced by each homeless subpopulation (especially homeless veterans), and a description of the means to be used to distribute grant amounts to sub-grantees. If the chief executive officer of a jurisdiction alters the comprehensive homeless assistance system description prepared by the board, the comments of the board on those changes will also be included in the application.

Ten percent of the overall HAF formula allocation will be used to create a bonus pool for excellent performance. The Secretary can also decrease the amount of a formula grant to a locality or State based on a review of the application and comments received from the community or as a result of the annual performance review and audit under the requirements of the fund. Alternatively, the Secretary could either (a) distribute the grant amounts by competition in that jurisdiction or (b) designate the State or a local private nonprofit organization to administer the grant amounts in that jurisdiction. Recipients will be subject to a maintenance-of-effort provision as well as a 25 percent match requirement for grants made available under the HAF, with appropriate match reduction waivers by the Secretary in cases of fiscal distress.

Transition

It is anticipated that the HAF will transition into the AHF by the year 2000. The Secretary will be authorized to accelerate the transition to AHF, when deemed appropriate, for communities that have succeeded in establishing a continuum of care for the homeless. During the transition period, localities will be able to map out and put in place comprehensive homeless assistance systems designed to coordinate and leverage resources, particularly resources from mainstream housing and services programs. These comprehensive systems for homeless care will inspire cooperation, encourage innovation, and demand coordinated action.

D. Housing Opportunities for Persons With AIDS

Persons with HIV/AIDS face unique challenges that have prevented access to safe, decent, affordable housing. These persons have increased health care and prescription costs while often losing income and support which results in homelessness or a high risk of homelessness. Mainstream housing programs have not adequately addressed the housing needs of persons with HIV/AIDS because of such issues as discrimination against persons with HIV/AIDS, fear of and misinformation about the disease, rapid impoverishment of persons with HIV/AIDS, lack of identified residential programs for these persons, increasing numbers of persons with HIV/AIDS with substance abuse problems, shortages of mental health and substance abuse residential treatment beds, and limited local capacity to expand housing options with appropriate services.

Communities are also challenged as the epidemic spreads. The increasing numbers of persons living with HIV/AIDS have challenged the abilities of programs with limited funding for services and housing assistance. Many volunteer efforts by community-based organizations are operating beyond their capacity and are forced to limit assistance to needy persons with the most severe difficulties.

The shortened life expectancy of persons living with HIV/AIDS and their specialized services needs together create an immediate need for housing which is particularly acute In Dallas, one HIV/AIDS service provider has served over 500 clients with HIV/AIDS Of 542 clients who qualified for Section 8 housing, only 1 ever received assistance under this mainstream program For others, the prospect of a multiyear waiting list was an eternity.*

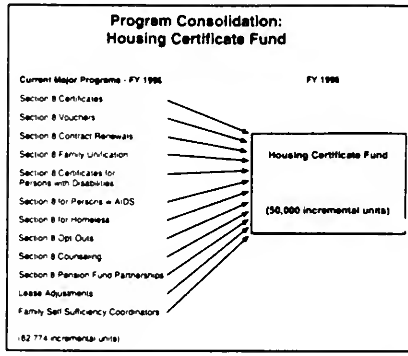
The Housing Opportunities for Persons with AIDS (HOPWA) program was created in 1992 to provide communities with a tool that addresses both the increased need for resources and the need to better plan and coordinate existing public and private efforts. HOPWA has given flexibility to communities in organizing their efforts and determining what types of activities and forms of housing will best help their residents who are living with HIV/AIDS In addition to financial resources, the program has created a statutory basis for the use of funds to address a targeted population of vulnerable persons. A locality's Consolidated Plan serves as the application, planning, and reporting mechanism for formula-distributed HOPWA funds, thereby providing a vehicle for coordinating HOPWA and other affordable housing efforts.

The HOPWA program will continue to operate as a separate program in fiscal years 1996 and 1997. Under the proposed consolidation, in 1998, HOPWA will become part of AHF, with any appropriate modifications to performance measures or the formula distribution made to reflect the consolidation at that time This 2-year transition for HOPWA is needed to ensure that newly supported AIDS housing efforts have sufficient time to strengthen their operations and increase their integration with other community housing and development efforts.

This transition is also necessary because HIV/AIDS housing development and planning under HOPWA has only been available since the fall of 1992. In many communities, the initial planning efforts and selection of project sponsors have only recently resulted in fully operating housing programs. The transition will allow these communities time to assess how these programs have benefited clients, make improvements, and further build the organizational capacity of the non-profit sector.

E. Housing Certificate Fund

A central element of HUD's mission is to increase opportunities for all Americans to obtain decent, affordable housing. The Department must pursue the most effective avenue to carry out this mission, based on a clear understanding of the real causes of housing problems in America and without regard to vested interests in existing and potentially outmoded programs The proposed Housing Certificate Fund (HCF) represents one such avenue, and an important one.



The primary source of severe housing problems in the U.S. today is lagging household incomes and high housing costs, not broad-based housing shortages. Decent housing is available; some households just cannot afford it. In fact, the vast majority of households with acute housing needs live in adequate, uncrowded housing, but are paying large portions of their incomes for rent. In 1993, for example, 5.6 million households had "worst-case" needs, which Congress defines as households paying more than 50 percent of their income for rent or living in substandard housing. Four out of five of these households live in housing that is both adequate and uncrowded; affordability is their only housing problem. The HCF will provide an effective tool to address this problem because it will make private housing affordable.

* According to this HIV/AIDS service provider, since 1990, of over 400 clients who qualified for Section 8 rental assistance, none survived long enough to make it to the top of the waiting list

Two decades of experience with HUD's Section 8 certificate and voucher programs have shown that tenant-based housing assistance is an extremely effective mechanism for meeting the urgent housing needs of low-income renters. This form of assistance empowers most recipients to find in the marketplace decent and affordable housing that meets their families' needs. A 1994 study of certificate and voucher recipients in 33 large urban areas found that 80 percent were successful in obtaining private market housing.

Tenant-based assistance also offers the potential to empower households to make the transition from renting to homeownership. For households who are prepared to assume the responsibilities of owning, certificates can be used for mortgage payments instead of rent. This feature of the HCF provides an opportunity for households already receiving rental assistance to "graduate" to assisted homeownership as their incomes rise, and creates a powerful incentive for responsible behavior and progress toward economic self-sufficiency.

Today's programs for tenant-based housing assistance leave significant room for improvement, however. The existing system does not work as well as it should — for housing authorities, landlords, or low-income families. As a result, not all subsidy recipients are successful in using certificates and vouchers, and there is growing evidence of significant barriers to full and free housing choice, especially for minority participants in the program. For example, white households are much more successful than black households in using their Section 8 certificates outside poor and minority neighborhoods. A recent General Accounting Office (GAO) study found that 55 percent of white recipients but only 36 percent of black recipients live in neighborhoods where fewer than 10 percent of the residents are poor.

Recent experience indicates that tenant-based housing assistance can be effectively supplemented by landlord outreach and housing search assistance to expand opportunities for choice and mobility. Over the past two decades, special mobility programs to help Section 8 recipients find housing have been implemented in at least eight metropolitan areas. These programs have helped roughly 11,000 families (about half in Chicago) move to low-poverty, low-minority neighborhoods, demonstrating that it is possible to help families take full advantage of housing, job, and social opportunities available throughout the regional private market, helping them to break out of the cycle of poverty.

This proposal builds upon the best features of the existing certificate and voucher programs but proposes changes to make the system simpler and more effective.

The HCF will exploit the full potential of tenant-based housing assistance, empowering households to choose moderately priced housing of the type and in the location that best suits their needs, encouraging upward mobility and homeownership, and attracting additional owners of private-market rental housing to participate in the program.

The proposal will consolidate the existing voucher and certificate programs and replace other project-based assisted housing programs including: Section 8 New Construction and Substantial Rehabilitation; Loan Management Set-Aside, Property Disposition, and Preservation; Rental Assistance; and Rent Supplement programs. As contracts expire on existing project-based programs and as public housing is transformed from a project-based system, HCF will become the vehicle for providing portable subsidies for low-income Americans. The HCF will be targeted to households with incomes of up to 50 percent of area median income, and subsidies will be calculated on the basis of HUD-determined Fair Market Rents (FMRs), set at the 40th percentile of rents for standard quality, recently occupied units in the local market area.

Key features of the new Housing Certificate Fund will address weaknesses of the current system. The HCF will simplify and standardize the application process and make it easier for recipients to use their assistance to move from one jurisdiction to another. Moreover, HUD will provide performance bonuses and increased flexibility for jurisdictions that participate in metropolitan mobility strategies.

Public housing authorities (PHAs) in metro areas with concentrated poverty will receive supplemental administrative funding to subcontract for family counseling, recruiting landlords into the program, and providing families with housing search assistance. The same PHAs will be required to use a portion of turnover and incremental assistance for moves from high-poverty to low-poverty neighborhoods to reverse the devastating effects of concentrated poverty and to avoid reconcentration of assisted households in marginal neighborhoods.

The HCF will eliminate burdensome program requirements that have discouraged landlords from participating in the Section 8 program, such as the "take one, take all" requirement (landlords who accept one recipient must accept all qualified recipients) and the "endless lease" provision that prohibits landlords from terminating leases except for cause or specific business reasons.

The new approach will encourage and reward work and other self-sufficiency efforts. It will allow PHAs to issue up to half of their certificates to working or work-ready

families in preference to other households. And it will require nonworking, able-bodied assistance recipients to perform community work. Up to 10 percent of incremental and turnover certificates may be set aside for households from special-purpose waiting lists, such as graduates of transitional housing programs for the homeless and participants in welfare-to-work programs.

The HCF will also enable and encourage households who are equipped to make the transition from assisted housing to homeownership. All families will be permitted to use their certificates to become homeowners instead of paying rent. In addition, PHAs will have the flexibility to develop local programs that help low-income families make the transition to homeownership. For example, localities could set aside a portion of their certificates for special-purpose waiting lists in connection with homeownership programs (within the overall 10 percent cap on the use of special-purpose waiting lists). They might also coordinate this assistance with housing rehabilitation funded by their Affordable Housing Fund (AHF). Note that participants drawn from a special-purpose waiting list for homeownership could have incomes up to 60 percent of area median income, higher than the income ceiling for the basic HCF program.

PHAs will have greater flexibility under the HCF, but will be held accountable for achieving measurable outcomes and meeting explicit performance standards. The HCF will impose financial penalties on a PHA that fails to achieve basic program performance standards and will authorize HUD to fund an alternative administrator if a PHA consistently fails to meet performance requirements. In addition, the HCF will provide bonus funding for PHAs that meet and exceed performance standards, and the Secretary will have the discretion to waive program requirements for localities, consortia, or States that submit innovative proposals for alternative mechanisms to satisfy HUD's performance standards.

Simplification, Flexibility, and Efficiency

The HCF will change requirements that have discouraged broader landlord participation, and will allow localities greater flexibility to coordinate their housing strategies with other local initiatives.

To encourage greater landlord participation, certain burdensome requirements will be eliminated. The "take one, take all" requirement will be dropped. The prohibition against lease termination for reasons other than good cause or verified business reasons will be eliminated (families living in public or assisted housing at the time of the transition will continue to be covered by this prohibition as long as they continue to live in these projects). The requirement that residents receive 90 days' notice before lease termination for business reasons will also be eliminated. In addition, landlords will be permitted and encouraged to screen certificate holders on the basis of performance-based standards of occupancy, as long as the screening complies with fair housing laws. Finally, families evicted from their units for serious lease violations will also lose their certificates.

Localities will enjoy significant flexibility in administering their programs. Each PHA will be required to develop a strategy for the local utilization of HCF resources, and this strategy will be incorporated into the Consolidated Plan for the locality (or State):

- Consolidated Plans will reflect local needs for tenant-based assistance and will enable localities to identify specific populations or geographic areas of need in which tenant-based assistance will not be effective. Where significant shortages of units are identified, high-performing PHAs will be permitted to transfer up to 15 percent of their HCF funds to the jurisdiction's Affordable Housing Fund (AHF) to provide project-based operating subsidies for housing production targeted to very low-income households.

- Well-performing PHAs will also have the flexibility to set aside up to 10 percent of incremental and turnover certificates for special-purpose waiting lists, encouraging coordination of HCF with other State and local housing assistance initiatives and designing locally appropriate homeownership models.

- More flexible program design will enable PHAs to address their unique circumstances and priorities. PHAs could adjust the definition of income used for calculating rent (exempting a portion of employment income or providing deductions for work-related expenses, for example) to give incentives to working families. And while HUD will continue to establish a national Housing Quality Standard, PHAs will be permitted to substitute local housing codes if they are at least as stringent.

- To enable PHAs to tailor their programs to local need, the existing Federal preference system will be replaced. In its place, PHAs will be permitted and encouraged to grant preferences for at least one-half of each year's admissions to families with locally defined "urgent housing needs." These preferences must be related to housing needs as described in the locality's Consolidated Plan. In addition, as noted above, up to half of all admissions can be families working toward economic independence. However,

to make sure no eligible families are completely excluded by preference systems, at least 10 percent of admissions must be families taken on a first-come, first-served basis from the PHA's waiting list

- Resources to expand local HCF programs will be allocated on the basis of need. The current "fair share" approach, which allocates assistance to HUD field offices and then holds competitions within allocation areas, has resulted in a disproportionate allocation of funding away from the areas of greatest need. To redress historical imbalances, HUD will annually recapture a portion of certificate turnovers, which — together with any incremental certificates funded by Congress — will be allocated to localities by a formula that reflects the eligible population with severe needs for assistance, as defined by the most recent available Census data.

- PHAs will be permitted to make adjustments to rent and subsidy levels to honor pre-existing commitments, e.g., to families under the Family Self-Sufficiency Program and to owners of units developed with project-based assistance under the HOPE VI Plus program, or similar initiatives.

PHA Rights and Responsibilities: Basic Program Requirements

Qualified PHAs will administer the HCF program. PHAs will receive an administrative fee that will no longer be tied directly to Fair Market Rents (FMRs). This fee system, described in HUD budget proposals for FY 1995 and FY 1996, will reimburse PHAs fairly in both low- and high-cost housing markets and in different types of service delivery areas, including geographically dispersed non-metro areas. Fees will be adjusted each year by a wage index rather than a rent index.

Administrative fees will cover direct HCF administrative costs (such as taking applications and managing waiting lists), plus subcontracts for landlord outreach and household search assistance. PHAs that both administer the HCF and own units in which certificate recipients live will not be permitted to perform unit inspections or rent determinations, because of the potential for a conflict of interest. These functions will be the responsibility of the local jurisdiction, and separate funding will be provided.

Incremental certificates, some recapture of turnover certificates, and certificates for families living in public housing and assisted multifamily projects will be allocated based on FMRs minus 30 percent of the estimated average gross income of program participants. Amendments under the Sections 8, 202, and 811 programs will be funded separately. A $25 million set-aside from each year's funding will provide technical assistance to resident associations and resident management corporations so that they can continue to serve families in former public housing developments that have been converted to tenant-based assistance.

Performance Standards and Bonuses

Assessments of PHA performance will be based on meeting minimum Federal requirements and achieving progress toward key federal program objectives. Minimum Federal requirements will include housing quality, fair access for protected classes of households, rent reasonableness, and the accuracy of income eligibility and tenant payment determinations.

In addition, while PHAs will be permitted to design their own adjustments to gross income, and in some circumstances adjust their rental payment standards from FMRs, the number of assisted families must total at least 90 percent of the number for which HUD bases its funding allocation to the PHA. This requirement is necessary to prevent PHAs from providing very large subsidies to only a few families, leaving extensive unmet needs. Similarly, to ensure that assisted households do not bear excessive rent burdens, a further performance standard will require that no more than 10 percent of assistance recipients pay above 35 percent of their gross income for housing. This requirement is necessary to prevent PHAs from creating a program that provides excessively shallow rental subsidies that are insufficient to give households access to decent housing at an affordable rent-to-income ratio.

PHAs failing to comply with federal performance requirements will bear the costs associated with remedial action to satisfy them — e.g., by using administrative fees to pay the costs of assistance to ineligible families where PHA error rates on income eligibility determinations exceed a HUD-determined maximum. For PHAs that consistently perform poorly, HUD will have the authority to pre-empt State law and turn the administration of the program over to high-performing neighboring PHAs or to establish a competitive process to identify alternative administrators.

High-performing PHAs will receive bonus funds based on an annual allocation of the greater of up to 15 percent of incremental and recaptured turnover funds or 1.5 percent of funds allocated for the total certificate program. To be eligible for these bonuses, PHAs will have to meet minimum program requirements and high performance standards. An example of such a performance standard is having a specific percentage of families with working-

age members showing increased efforts toward self-sufficiency, as well as outstanding performance in other aspects of the program. As discussed earlier, high-performing PHAs will also be permitted to transfer up to 15 percent of incremental and turnover funds to the Affordable Housing Fund (AHF) when a need for operating subsidies for housing financed in part through the AHF is identified in the locality's Consolidated Plan.

Family Choice

The current project-based housing assistance system prevents low-income people from freely choosing where to live. Where subsidy is linked to a project, low-income people are effectively compelled to live there, regardless of safety, suitability, proximity to family support systems, or access to employment opportunities. Even under current tenant-based assistance programs, prospective tenants may be denied the opportunity to move outside their jurisdiction because surrounding PHAs have separate waiting lists and preference systems. The HCF proposal will offer eligible needy Americans a real choice and a real opportunity to escape from concentrations of poverty:

- It will establish a single, standardized application for all PHAs administering the program, thereby ensuring that applicants need not fill out separate forms to apply for assistance in different jurisdictions. PHAs will be required to accept applications by mail.

- Recipients of assistance will be permitted to use their certificates for any housing unit that otherwise satisfies program requirements, regardless of its rent level.

- With the exception of certificates that a PHA targets to special waiting lists, recipients will be permitted to use their certificates anywhere, regardless of where they applied for assistance or where they lived when they received the assistance.

- Eligible households will be permitted to apply for housing assistance in any jurisdiction they wish, and must be treated the same as similarly situated applicants who already live in that jurisdiction. Currently, jurisdictions have the authority to grant preferences to their residents. These preferences have the effect of limiting access to assistance for needy families, and creating barriers to mobility and choice. Therefore, residency preferences will no longer be authorized.

- One of the performance standards used as the basis for awarding bonus funds will reflect success in marketing the program to a broad range of landlords and helping families locate housing in areas of low poverty.

- For urban areas with concentrations of poverty, PHAs will be required to subcontract with qualified mobility counseling agencies for landlord outreach, family counseling, housing search assistance, and other activities that maximize opportunities for assisted families to move to low-poverty areas. PHAs will receive supplemental administrative funding for this subcontracting.

- To increase the number of families moving out of severely distressed, high poverty areas, HUD will be authorized to require cities with severe concentrations of poverty to use a specified portion of the PHA's certificates to enable families with children to move from high-poverty to low-poverty areas. Families receiving these certificates (whether they are drawn from the waiting list or already receive rental assistance) will also receive mobility counseling and search assistance.

- In addition, PHAs that participate in metro-wide mobility plans will be eligible for bonus allocations of certificate funds as well as for the flexibility to use 10 percent of certificates for special waiting lists and to transfer 15 percent of certificate funds to the AHF. PHAs participating in metropolitan mobility strategies must implement a metro-wide waiting list and honor the preference rankings of other participating jurisdictions.

Family Eligibility, Rights and Responsibilities

Nationally determined eligibility requirements will ensure that assistance goes to those in need. Families admitted will be required to have incomes below 50 percent of area median income (except for first-time homebuyers drawn from special-purpose waiting lists, in which case the income ceiling is 60 percent of area median). Gross income ceilings will be calculated by HUD, with adjustments to ensure that poor working families are not unfairly excluded in unusually low-income areas and that certificates are made available to all needy families in high housing-cost areas. Certificates will be made available to all families residing in public housing or project-based assisted housing when it is converted to tenant-based assistance, unless their incomes exceed 50 percent of area median and they are already paying market rents no greater than 30 percent of their income.

Under HCF, increased family choice will be accompanied by clearer tenant responsibilities. These include:

- Low-income families will no longer be able to retain their subsidy and use it in another unit if they are evicted for serious lease violations.

- Landlords will be encouraged to require families to comply with basic admissions requirements. Families could, in fact, be denied a unit based on previous behavior such as not paying rent and other charges in a timely manner, not caring for the unit, interfering with others, engaging in criminal activity, using or selling drugs, and failing to comply with reasonable rules and requirements. PHAs will, however, be required to help families with potential fair housing complaints if such standards are used in a manner that discriminates illegally under the Fair Housing Act.

- Program participants will be required to contribute a minimum of 8 hours per month in work within their community. This community work requirement will ensure nonworking assistance recipients to contribute to the well-being of their community, and may help them make the transition to the world of work. Exemptions will be provided for those who are elderly or severely disabled, or who already meet welfare work requirements.

- Tenants will receive a financial incentive to choose lower priced units. Specifically, they will receive a reduction in their contribution to rent if they select housing that rents for less than the FMR. This "shopping incentive" will encourage tenants to search for and negotiate the best rent bargains they can, and will help prevent rents from automatically rising to the FMR.

Chapter Two:
Public and Indian Housing Transformation

The second component of reinvention is a dramatic transformation of public housing. Since 1937, the Federal Government has invested some $90 billion in the public housing inventory. The legacy of this investment is mixed.

On one hand, public housing provides a stable supply of rental housing that is affordable to families with very low incomes. Approximately 1.3 million households live in public housing developments operated by some 3,400 public housing agencies. Approximately 45 percent of these households are families with children, 35 percent are elderly, and another 10 percent are disabled.

For these households, public housing provides a real, tangible response to the failure of the private market to provide sufficient housing at affordable rents. In some communities, public housing accounts for as much as 15 percent of all rental housing and a much higher percentage of the low-rent stock (i.e., carries rents of $350 per month or less that are affordable to low-income families).

Despite serving this critical function, the current public housing system is plagued by a series of deeply rooted and systemic problems. These problems exist in projects of national infamy — Robert Taylor Homes in Chicago, Desire in New Orleans — as well as in hundreds of small-scale developments. They exist in the 100-odd public housing agencies that have severe management deficiencies as well as in the overwhelming number of agencies that operate efficiently. Change, therefore, must be far-reaching and comprehensive if it is to be successful.

The structural problems of public housing are multiple.

Public housing denies residents the right to choose where to live. Public housing ties subsidies to specific units and projects; residents receive the benefit of the federal subsidy only if they agree to live in a specific public housing unit. Resident choice is limited, therefore, to whatever unit of the right size happens to be available when their name reaches the top of the waiting list, irrespective of whether that housing best suits their needs.

Federal laws have concentrated the very poor in public housing. The average income of families living in public housing is currently around 17 percent of area median income or $6,100. This is a relatively recent phenomenon. In 1980, for example, the average income of families living in public housing was around 33 percent of area median income. Congressional decisions during the past decade-and-a-half — particularly federal laws governing admissions and income targeting — compelled public housing agencies to serve those low-income families experiencing the greatest distress.

Local officials have sited public housing developments in high poverty areas. The poverty and distress of public housing residents is exacerbated by the tendency of public housing to be located in areas lacking jobs and economic opportunities. These neighborhoods generally lack basic amenities; transportation and other urban services also tend of be of diminished quality. The location of public housing, of course, is not accidental; the siting of developments during the 1950's and 1960's was often the result of deliberate decisions to segregate.

The public housing experience contrasts sharply with that of the Section 8 certificates and vouchers. A recent General Accounting Office (GAO) study of four metropolitan areas indicated that fewer than 10 percent of Section 8 recipients live in high poverty neighborhoods (i.e., neighborhoods that are more than 30 percent poor). In contrast, 23 percent of public housing residents live in such high poverty neighborhoods. Blacks who receive tenant-based assistance are far less concentrated in high poverty, high minority neighborhoods than those who live in public housing.

Federal laws penalize public housing tenants who work. They discourage unemployed families from working and working families from staying. Public housing rents, set at 30 percent of a family's adjusted income, penalize families who want to work — by taking away 30 cents of every additional dollar they earn and a higher portion of their after-tax income. In addition, rents charged for families who are already working are often far higher than that which the unit would command in the private market, since rents are based purely on income. As a result, residents who would provide the best role models are often those who leave at their first opportunity.

The discipline of the real estate market does not apply to public housing. The current system empowers a distant, Federal bureaucracy to ensure that public housing agencies perform well in maintaining and administering their housing stock. Residents who are in the best position to identify management deficiencies and compel changes are denied the ultimate tool available to consumers, i.e., the ability to take their

business elsewhere. No matter how poor the physical condition of the apartment, no matter how crime-ridden or economically distressed the neighborhood in which the housing is located — subsidies are tied to public housing units and cannot be transferred.

The Federal method of overseeing the public housing industry aggravates the problem. Federal statutes and rules regulate every aspect of public housing, including admissions, rents, evictions, resident rights and relations, modernization, development and procurement. The system is awash in process and paperwork, in adhering to guidelines and filling out forms. These layers of bureaucratic complexity place excessive administrative burdens on all public housing agencies, particularly those that are small.

The lack of market controls is evident in the rising cost of public housing. Public housing is a self-contained system where decisions on operations and rehabilitation are made without any market test or constraint. Agencies that want to tear down housing that is no longer viable are thwarted by statutory provisions that require one-for-one replacement of demolished housing and by the lack of sufficient resources for such replacement. Agencies that want to create living environments that are economically diverse are thwarted by admission rules that favor those families with the lowest incomes and most urgent housing needs. Agencies that want to acquire or build small-scale affordable housing are thwarted by rules that prevent agencies from acting in a time-certain manner, critical in real estate.

It is not suprising that the average appropriation per occupied unit of public housing has increased to $481 per month, compared to $440 per month to serve these same households with rental certificates in the private market. The higher public housing subsidy reflects the rising cost of operating properties that serve the very poor, modernizing projects that have deferred maintenance for years, combating crime and drug activity in and around densely concentrated developments, and addressing the various social needs of residents.

Over the past two years, HUD has undertaken a concerted effort to address the problems in the current system.

- To foster greater economic integration, HUD changed the admission rules governing permit agencies to favor working families when filling vacancies.

- To make work pay, HUD proposed sweeping changes in public housing rent rules — which Congress supported but never enacted.

- To generate opportunities for residents, HUD expanded youth apprenticeship efforts, increased support for resident councils, and linked modernization funding to jobs for residents.

- To fight violent crime and drug trafficking, HUD and the Treasury and Justice Departments have started pooling and coordinating their efforts for the first time under the Operation Safe Home initiative.

- To turn around troubled public housing agencies, HUD continued or initiated comprehensive recovery efforts in Philadelphia, New Orleans, Washington, D.C., Detroit, Kansas City, Chester, and Chicago.

- To end Federal micromanagement, HUD streamlined and simplified the rules governing nearly every aspect of public housing management, eliminating dozens of handbooks and guidelines in the process.

- To end wasteful support for distressed public housing, HUD accelerated the demolition, reconstruction and/or replacement of some of the worst public housing developments in the nation.

Much has been accomplished in the past 2 years. In community after community, public housing is becoming safer, more livable, an engine for community revitalization rather than neighborhood decline. Yet, in the final analysis, these positive steps are incremental in nature and cannot succeed in changing the fundamental, structural problems — the denial of resident choice, the concentration effects, the lack of market discipline — that permeate our nation's public housing.

The reinvention proposal for public housing is simple yet profound. Where the current system funds bureaucracies, we will fund people. Where the current system gives public housing agencies capital and operating subsidies to maintain projects, we will give families rental vouchers — modeled on the Section 8 program and pegged to the local cost of decent housing — that could be used in public housing or a private apartment of their own choice. Where the current system relies on a complex, complicated array of rules and regulations to oversee the performance of agencies, we will rely on families to decide whether management has performed well.

For the first time in 60 years, public housing residents will enjoy the same privilege that all of us have — the freedom to choose where they live. If they don't like the housing offered by housing agencies, they will be able to move. Housing agencies will have to compete for their business, just like private landlords. Well-managed authorities will survive; poorly run authorities will have to shape up or go under. Success will be determined, not

Moving Out of Public Housing: A Chicago Success Story

Arletta Jackson is a single mother who used to live in Ida B. Wells, one of the grim, high-rise public housing projects that march for miles along Chicago's South Side. When Arletta Jackson lived at Ida B. Wells, she didn't have a job. There were no jobs in that community. She used to fear for her son's life each time he went outside to play there. Every time she heard a car backfire, she would rush to the window, thinking it was gunfire — fearing that her boy had been shot.

Today, Arletta Jackson does not have to worry about her son getting shot anymore. Because of a federally supported housing certificate program, she and her son were able to move out of Ida B. Wells, to Hoffman Estates, a safe suburban community where there are good schools and job opportunities. And today, Arletta Jackson herself is self-supporting; she has a job at Ameritech. And her son, Jason, plays the flute in the school band. They are in the mainstream of life now, and moving toward a much better future.

by top-down rules and regulations that focus on process rather than results, but instead on bottom-line outcomes as determined by the residents themselves.

The reinvention proposal will expand federal efforts to reward work and treat housing as a starting place for personal and family mobility and self-improvement. Localities will be permitted to provide special incentives and preferences for families that are engaged in self-sufficiency efforts. Able-bodied residents who are not working will be required to work in their communities. Support for resident organizing and organizations (particularly resident management corporations) — which complement the new emphasis on work and responsibility — will continue at substantial levels. Innovative uses of the new rental subsidies for homeownership purposes — and creative configurations of ownership and management among public housing agencies and resident groups — will be encouraged.

What will be the likely outcome of this radical change? Most public housing residents will be able to stay in their current housing, and many will choose to do so. Those whose developments are demolished will be guaranteed relocation, either with a certificate or where that is not their preference, to other public housing units. Residents who wish to remain in public housing will continue to benefit from lease protections. Families who remain in former public housing projects and those who move elsewhere will both have new opportunities to live in mixed-income communities.

The former public housing stock will become an important housing resource, adding to the already substantial private market of available rental units for both subsidized and unsubsidized families. Success rates in the certificate and voucher programs have been increasing steadily over time. Recent studies show that 80 percent of those who try to use tenant-based assistance in large urban PHAs are successful in finding units that qualify for assistance, even without the current public housing stock as one of their choices.

These findings are not surprising since in most housing markets there is an adequate supply of housing **available for certificate recipients**. Although there are indeed shortages of low-cost housing in most urban housing markets, these shortages generally occur at the very low end of the rental market — well below the Fair Market Rent (FMR) calculated at the 40th percentile of recently occupied, good quality units. Analysis of Census data for 13 metro areas shows that at least 40 percent of all 2-bedroom units rent at or below the FMR. Moreover, these data show that units renting for less than the FMR are quite widely dispersed geographically, accounting for at least 30 percent of the rental stock in over two-thirds of all residential Census tracts.

This reinvention plan will work for the overwhelming majority of public housing agencies that are not troubled. These agencies will, for the first time, be able to market their housing to a broad range of subsidized and unsubsidized families, make their own choices about which units to rehabilitate, and target their activities to local needs. Freed of Federal micromanagement, agencies will be in a position to be innovative and creative, deploying federal resources based on their local circumstances and coordinating the public housing system with the localities' larger affordable housing, homeownership, and community development strategies.

Housing Certificate Fund:
Tenant-based housing assistance has proven to be an extremely effective mechanism for meeting the urgent housing needs of most low-income renters.

The majority of households who receive Section 8 Certificates and Vouchers are successful in finding units that qualify for assistance.

- HUD conducted a nationwide study of the Section 8 Certificate and Voucher programs, completed in 1994, which found that 80 percent of program participants who live in large urban areas are successful in locating housing.
- About one-third of the program recipients use their assistance in-place — they already live in adequate housing, and tenant-based assistance allows them to reduce their rent burden.
- Even among those who have to move to qualify for the assistance, 52 percent are successful nationwide.
- Success rates in the Certificate and Voucher programs have been increasing steadily over time, indicating that the program is becoming easier to use as landlords and PHAs become more familiar with it.

In most housing markets, there is a substantial supply of housing at rents around the Fair Market Rent (FMR).

- Analysis of Census data for 13 selected metropolitan areas shows that at least 40 percent of all 2-bedroom units had rents at or below the FMR.
- According to the data, in each of the 13 metropolitan areas, units renting for less than the FMR are widely disbursed geographically, accounting for at least 30 percent of the rental stock in over two-thirds of all residential Census tracts.

Clearly, change of this fundamental nature cannot be accomplished overnight. The number and intense poverty of public housing residents — and the fragility of neighborhoods in which public housing is located — caution that change be phased over time to ensure that vulnerable families are not harmed.

The reinvention proposal envisions an orderly and prudent transition to prepare agencies and residents for the shift to a market environment. Small public housing agencies will convert to the certificate model by the end of three years. For larger public housing agencies, a six-year, three-part transition is envisioned during which period good public housing will be made marketable and nonviable stock will be demolished.

During the first transition stage, beginning in fiscal 1996, HUD will consolidate dozens of disparate public housing programs into two accounts, one for capital and management improvements, one for operations. HUD will also decontrol and deregulate the 3,300 public housing agencies that are performing well. Federal micromanagement will be supplanted by local bottom-up planning and flexibility, enabling PHAs to utilize their resources to best meet local needs and opportunities.

All agencies will be given the flexibility to determine which units to modernize and which to demolish, providing incentives for quick demolition of some of the most distressed units. With the worst public housing demolished, PHAs will then have the flexibility to make the remaining public housing stock generally competitive.

HUD will turn its attention towards those 100 agencies that continue to exhibit severe management deficiencies. New, enhanced receivership powers will be sought, giving HUD the ability to intervene aggressively in these perenially "sick" agencies.

Metropolitan Areas	Number of Census Tracts with at Least 10 Two-Bedroom Rental Units	Number of Census Tracts with at Least 30% of Two-Bedroom Rental Units with Rents Less than 40th Percentile FMRs	Percentage of Census Tracts with Rents Affordable at 40th Percentile FMRs
Atlanta, GA	436	310	71%
Buffalo-Niagara Falls, NY	279	251	90%
Cedar Rapids, IA	40	37	93%
Columbus, OH	325	277	85%
Davenport-Moline-Rock Island, IA-IL	93	70	75%
Detroit, MI	1057	752	71%
Houston, TX	643	525	82%
Kansas City, KS-MO	406	332	82%
Nassau-Suffolk, NY	487	408	84%
New York, NY	2115	1927	91%
Seattle, WA	416	349	84%
St. Louis, MO-IL	457	383	84%
Wichita, KS	117	102	87%

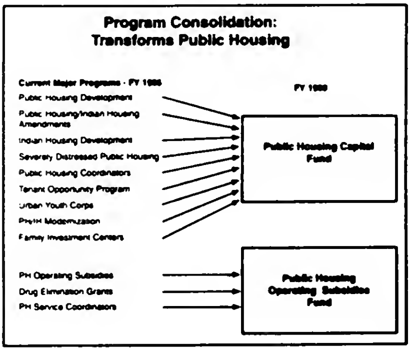
During the second transition phase, existing capital and operating subsidies will be converted to project-based assistance. This transition will give agencies experience with operating on a market discipline, where rents rather than arbitrary capital and operating budgets drive management of the property.

In the final phase, subsidies will be coverted to tenant-based assistance.

A. Public Housing Transformation

Stage I: Immediate Deregulation and Program Consolidation

The first stage will ensure that PHAs have the ability to demolish the worst public housing developments (the 80,000 to 100,000 units that are severely distressed), plus those that are so poorly located that they have no hope of charging market rents high enough to cover costs even after the development is rehabilitated and the PHA's operations are deregulated and streamlined. The PHA will develop a strategic plan, linked to the locality's Consolidated Plan, that will determine the role former public housing buildings should play in the overall local stock of affordable housing and will guide the PHA's investment decisions during the transition.



A Vision for Public Housing in Richmond, Virginia

In December 1994, HUD held its Annual Performance Awards Ceremony to honor innovative programs implemented by local housing authorities. The Richmond Redevelopment and Housing Authority (RRHA) received the "Innovative Housing" award for its visionary approach to public housing. RRHA's initiative to create, "Public Housing Designed to Improve the Neighborhood and Advance Homeownership," built 34 new townhouses to be purchased by low-income families, with priority given to former public and assisted housing residents.

The RRHA established its homeownership program in 1987 with CDBG funds allocated by the city. The program is now funded through innovative uses of public housing development and modernization funds. Working families, the target population for this program, undergo extensive homeownership training (i.e., maintenance and repair, personal budgeting, energy conservation) and, as further preparation, actually lease the property for at least a year before assuming ownership.

These townhouses, with a price range between \$50,000 – \$62,000, are the first new homes constructed in the Carver area of Richmond in 50 years. The new homes have revitalized an entire community. To further enhance the community revitalization in process, the RRHA also offered rehabilitation loans and grants to qualified, current homeowners in the neighborhood.

In June 1994, residents began moving into the Carver townhouses. To date, 32 of the 34 units are occupied. RRHA's Homeownership Program has enhanced the lives of the participants by encouraging them to set high goals for themselves. These goals do not stop at buying a home, but spill into other aspects of their lives, motivating them to develop higher aspirations for their personal lives. The sense of pride derived from being a homeowner gives them a feeling of independence and increases their self-esteem.

The Richmond Redevelopment and Housing Authority exemplifies the kind of innovative role that housing authorities across the country should be moving toward under the "new" HUD: creating public housing that serves as a launching pad to homeownership and self-sufficiency and contributes to the diversity and strength of mixed-income neighborhoods.

PHAs operating efficiently will gain more ability to become entrepreneurial. Troubled PHAs not already under receivership or conservatorship will be given one year's notice, after which takeover of their operations by HUD or another entity will be mandatory. A new, more rational series of incentives for PHAs and residents will build on the deregulation already underway, including changes in HUD handbooks, streamlined program rules, and revised annual contributions contracts.

All existing public housing categorical grants will be combined into two flexible funds — one for operating expenses and one for capital and management improvement needs.

Capital Fund

The Capital Fund will be modeled after the current comprehensive grant program. It will permit PHAs to bring as much as possible of their housing stock up to a standard that will attract and keep tenants at market rents that will cover ongoing costs. The Capital Fund will also be used for replacement housing. Eligible activities will include those currently eligible under modernization programs (both the Comprehensive Grant Program and the Comprehensive Improvement Assistance Program), under programs for distressed public housing developments (major reconstruction of obsolete projects and the HOPE VI program), and activities of the Family Investment Centers program. A reserve will be established for natural disasters, desegregation, technical assistance, and administration of troubled housing

In preparing a development-by-development strategic plan for getting ready to compete in the market, PHAs will be required to meet with all the local stakeholders — residents, elected officials, neighbors, and others. The strategic plan will identify projects to be demolished, the schedule for rehabilitation and transition for projects to be retained, the uses of the Capital Fund for management improvements and resident programs, and funding sources outside the Capital Fund that will be tapped for needed work. The strategic plan summary will become a part of the locality's Consolidated Plan.

The Capital Fund will use elements from the allocation formula of the Comprehensive Grant Program. However, because this consolidated program incorporates special programs designed to address the severe backlog of needs of distressed projects at some PHAs, the proposal will change the current 50/50 weighting of backlog versus accrual of need to one that is more heavily weighted on backlog. The current competitive Comprehensive Improvement Assistance Program for small PHAs (fewer than 250 units) will be replaced with a formula stream of capital funding in order to permit these authorities to plan in a coordinated fashion.

Because all eligible uses under the funds being consolidated will be incorporated into this larger fund, PHAs will have flexibility to choose from a broad menu of eligible activities. For example, the current eligible uses under HOPE VI, which permit funds to be used for supportive services, community service and economic development expenses, will now apply to the Capital Fund. In addition, the menu of eligible activities will be clarified to include funding of replacement reserves and non-routine maintenance, including planned code compliance programs.

Replacement housing produced under the Capital Fund will not be subject to the requirement for a Family Self-Sufficiency program for a number of units equal to the number being produced. However, PHAs already operating Family Self-Sufficiency programs will continue them during the transition.

Subjecting PHAs to market discipline will require informed and engaged residents who understand their choices. At the same time, former public housing developments will be more attractive to tenants, both subsidized and unsubsidized, if they have well-organized and active resident associations. Therefore, the greater of $25 million or one half of one percent of the Capital Fund appropriation will be provided competitively to resident organizations for activities currently eligible under the Tenant Opportunities Program. Residents will also continue to be protected by the tenant participation and elections rules promulgated by the Department in 1994 after extensive consultation with resident leaders

Operating Fund and Occupancy Standards

The operating fund will consolidate funding for anti-crime activities, service coordinators for residents who are elderly or disabled, and the existing operating subsidy fund. All existing eligible uses under these funds, plus expanded anti-crime activities, will be permitted. The existing Performance Funding System formula will be modified to include components reflecting these new activities (with the crime component targeted to PHAs in all larger cities and those smaller cities with significant crime problems as well as those who received Public Housing Drug Elimination Program or youth sports grants over the last three fiscal years).

There will be a set-aside from the Operating Fund performance bonuses to reward PHAs that are making particularly rapid and effective progress towards the transition to market-based rents. HUD's FY 1996 budget requested $172 million for this bonus fund.

PHAs must have the flexibility to begin to attract a broader range of families in order to be ready to compete for subsidized families who can use their certificates elsewhere, as well as unsubsidized families who will pay market rents. Therefore, during the first stage of the transition, PHAs will be permitted to adopt ceiling rents that reflect the market value of the housing and to permit families to pay those rents when 30 percent of the family's income would be higher. Such ceiling rents can be lower than those currently permitted for public housing.

To further encourage somewhat higher-income families to move into public housing and to encourage working families to stay in public housing as their incomes grow, PHAs will also be permitted to make adjustments to the income on which rent is calculated (for example, disregarding items such as payroll taxes). However, PHAs that choose lower ceiling rents or larger income disregards than those permitted by current law will not receive additional subsidy from the Operating Fund if lower rents charged are not offset by higher resident incomes. Instead, PHAs willing to assume this risk will have their operating subsidies "frozen" at a level based on their previous rent roll

In addition to reforms to rents charged during the transition, housing authorities will be permitted and encouraged to adopt a preference for families that are working toward economic independence — for example, families with adult members who are working, in training or education programs, or ready to work.

Other Reforms to Increase PHA Flexibility

The proposal will institute a series of reforms to increase PHA flexibility to operate, manage, and rehabilitate their stock. These reforms will enable PHAs to respond to the housing market needs identified by strategic planning and will end requirements that have left empty hulks of public housing buildings scarring the urban landscape. These changes include:

- The process for approving demolition of nonviable or unmarketable units will be simplified and expedited. Under this new, substantially less stringent test, demolitions will be permitted for buildings that will not be self-sustaining from market-based rents and thus would constitute an excessive drain on PHA resources.

- Existing statutory one-for-one replacement requirements will be repealed. Residents of demolished units will receive relocation assistance, which will include issuing a certificate (together with necessary counseling, outreach, and search assistance to assure successful placement) or providing the residents with another public housing unit or other replacement unit.

- The current requirement restricting the use of proceeds of public housing disposition will be amended so that PHAs no longer will be required to repay any outstanding bonds from past capital debt of the project. However, PHAs will continue to be required to use the proceeds for low-income housing.

- PHAs will no longer be required to meet Federal *and* State or local procurement requirements. Rather, this proposal will establish a Federal pre-emption during the transition to remove redundant requirements and permit PHAs to move quickly to make their stock ready for market competition.

- Existing lead-based paint requirements will be altered to achieve consistency with the requirements proposed by the lead-based paint advisory committee for private rental housing.

Performance Standards, Bonuses, and Troubled PHAs

PHAs will continue to be subject to the revised Public Housing Management Assessment Program indicators, which will be used to rate all PHAs at least annually as well as to identify troubled agencies. Where troubled agencies are identified, localities will be required to address in their Consolidated Plan how they intend to assist in recovery efforts.

Furthermore, the proposal will establish a benchmark of one year during which troubled PHAs must either improve or HUD will be required to find that the PHA has breached its contract with the Federal Government. HUD must administer the PHA, appoint another entity as conservator, or seek a court-ordered receivership.

When HUD takes direct control of a troubled PHA or establishes a conservator, it will have expanded powers. In addition to its current authority to abrogate contracts and to supersede state or local personnel, procurement, or other laws, HUD will seek authority to demolish buildings and to sell PHA assets. HUD will use technical assistance funds or funds from the Capital Fund reserve to create a corps of professionals or another entity with the skills to resolve and, where necessary, dispose of PHA assets.

Rights and Responsibilities of Tenants

The proposal reflects a recognition that tenant rights must be matched with responsibilities. As described above, during the transition families that work will be encouraged by PHAs that implement ceiling rents and earnings disregards. In addition, family members will receive job opportunities through application of the Section 3 requirements for expenditures under the Capital Fund during the transition and as long as it takes for any work started with those funds to be completed.

Families will be obliged under their lease to perform 8 hours per month of community work. Exemptions from this requirement will apply to the elderly, the severely disabled, and families meeting work requirements under welfare programs. In addition, PHAs will be permitted to charge a minimum rent, so long as that minimum does not exceed 30 percent of SSI for individuals or AFDC for families.

For states that provide due process legal proceedings for lease terminations (the vast majority of states), the mandatory grievance procedures will be changed. A streamlined, one-step grievance procedure will be mandated for disputes between the PHA or Resident Management Corporation and residents. The procedure will not be available to residents whose leases are being terminated for criminal activity or actions that pose a threat to the lives, health, safety, or property of other residents or the PHA or RMC. For states without due process procedures, the current grievance procedures will remain in effect.

Protection of Vulnerable Populations

PHAs must begin marketing their housing to a broader range of families in order to be in a position to compete for tenants at the end of the transition. However, it is also important to preserve access to the public housing stock and to the certificates that will be issued to families at the end of the transition, for vulnerable populations. The following provisions balance these considerations:

- During the transition, the income eligibility rules that apply to the Housing Certificate Fund — 50 percent of area median income except for families in special homeownership programs — will apply to public housing as well. This will supplant the current public housing admissions rules, in which some newly admitted families can have incomes between 50 and 80 percent of area median income. However, the more flexible system of preferences established for certificates will also apply to public housing and will permit PHAs:

  — to define acute housing needs with reference to the local Comprehensive Plan rather than automatically using the current system of Federal preferences that focuses on those with severe rent burdens (generally the poorest families);

  — for up to 50 percent of families admitted to public housing, choose families moving toward economic independence ahead of other families.

- Lease protections, including the ability to evict only for good cause, will continue during the transition. These protections will remain in effect after the transition for families who continue to live in their former public housing units.

- Federal restrictions will continue to apply, both during and after the transition, to the sale of public housing buildings or land on which public housing once stood. All such sales must be approved by the Secretary. This, along with continued lease protections, will ensure that the move to tenant-based assistance does not result in the displacement of very low income individuals and families from the best public housing sites.

- Prior to approval by HUD of *any* sale of public housing buildings or land, the property must be offered to resident organizations at market price for continued use as low-income housing. The resident organization will have 30 days to express interest and will have an additional 60 days to obtain a financing commitment. In addition, resident management corporations that are chartered as of a date one year after the passage of relevant legislation and are experienced in managing public housing will be offered property at no more than 75 percent of the market price.

- If an occupied development is sold to other than a resident corporation, the new owner will be required to continue to house residents under existing leases, which may not be terminated without good cause.

- Very low income elderly and disabled populations will receive special preferences for occupancy in buildings for the elderly, disabled or mixed populations. This will ensure that the very low income elderly are not replaced by higher income elderly persons.

<u>Stage 2: Market-based Rents With Project-based Assistance</u>

Under this stage, PHAs no longer will receive assistance under the Capital Fund or the Operating Fund. Instead, they will receive certificates from the new Housing Certificate Fund. These certificates will provide a level of subsidy based on the market value of the housing (not to exceed the Fair Market Rent used for the Housing Certificate Program), rather than on the needs-based formulas used for the Capital and Operating Funds. However, in order to give PHAs time to adjust to charging market-based rents and to permit the completion of rehabilitation work making the housing more marketable, during this stage of the transition subsidies will still be project-based. Families will not be able to take their certificate and move elsewhere. This project-based assistance will only be available for occupied units of standard quality.

For PHAs that both own public housing and administer the Housing Certificate Fund, the local government will have the responsibility for an independent inspection of the housing and determination of whether the rent charged is the equivalent of a market rent.

Both at this stage of the transition and after the transition to tenant-based assistance, market rents charged for public housing rents will be permitted to include costs of services provided and paid for by the PHA — such as child care and congregate meals, so long as those costs do not result in rents that are greater than the Fair Market Rents.

During this transition period, terms of the Annual Contributions Contract will be modified. Appropriate protections will be instituted to reserve units for very low income households and to continue the lease protections of current residents. Federal conditions on demolition and limitations on sale of property will continue. In

addition, families that would otherwise have incomes too high to qualify for assistance under the Housing Certificate Fund (i.e., families with incomes over 50 percent of area median income) will be eligible to receive continued assistance if their income-based rent is less than the market rent for a public housing unit in which they wish to remain.

In order to provide maximum flexibility to PHAs to establish mixed-income communities, vacated units will be made available during this stage of the transition either to families on the PHA waiting list who are eligible for the Housing Certificate Fund or to families who are not eligible for assistance but have incomes below 80 percent of area median income.

Stage 3: Market-based Rents With Tenant-based Assistance

During this stage, the Nation's public housing program will be replaced by a tenant-based subsidy system operated through the Housing Certificate Fund. PHAs will be landlords in the true market sense, and PHA units will represent one of the housing options available to low- and moderate-income Americans.

Certificates allocated for subsidizing public housing units under Stage 2 will continue, but they will now be attached to the family rather than to the public housing unit and the family will be free either to stay in public housing or to move to other housing qualifying under the rules of the Housing Certificate Program. These rules include:

- HUD will use the same Fair Market Rents system that applies to the general Housing Certificate Program, calculated as the 40th percentile rent for good quality units into which new families have moved in the past 2 years.

- A methodology will be established for determining reasonable market rents for participating units, within the overall FMR limits. That methodology will permit PHAs and other owners of former public housing developments, as well as other owners of rental housing, to charge rents that cover the costs of services provided and paid for by the owner, such as child care and congregate meals if that can be done within the FMRs.

- Residents who choose to move out of public housing will be permitted to use their certificates in any locality, regardless of where they lived when they received the assistance.

- Residents will be free to use their certificates at any housing unit that otherwise satisfies program requirements, regardless of its rent level.

- Families will receive a financial reward for renting lower-cost units, including former public housing units, if those units pass the housing quality standards and meet the family's needs. This "shopping incentive" will be important in enabling public housing located in modest neighborhoods and built to design standards of an earlier era to compete with other rental housing that may be available to families with certificates. The shopping incentive will be a reduction in the family share of rent calculated by the percentage that the unit rent is less than the FMR.

- The administrator of the Housing Certificate Program will often be the same PHA that continues to own former public housing developments. However, in order to avoid conflicts of interest, the local government will be responsible for the housing quality inspection and rent reasonableness functions.

- PHAs will be permitted to make adjustments to income used for determining the certificate subsidy amount, for example for expenses associated with working. Funds for these certificates will still be allocated from HUD to the PHA as though the subsidy were the difference between FMR and 30 percent of gross income.

- PHAs will be permitted to adjust FMRs upward when necessary to make a broader range of housing and neighborhoods available to families. This flexibility will be controlled by performance requirements that ensure that PHAs do not set subsidies so high as to curtail the number of families assisted or so low that many families are paying over 35 percent of their income for housing.

- Former public housing residents using certificates, whether in public housing or in other parts of the rental housing market, will be required to contribute a minimum of 8 hours per month of community work, with appropriate exceptions for the elderly, or severely disabled, or families who meet the work requirements under welfare programs.

- Landlords, both owners of former public housing developments and other landlords of families using certificates, will be permitted and encouraged to require families to comply with basic admissions requirements. Low-income families will no longer be able to retain a certificate subsidy if they are evicted for serious lease violations.

In some circumstances public housing developments designated for occupancy by elderly and disabled residents will receive special protections to ensure their financial stability after the transition to tenant-based assistance. Instead of permitting all residents of such projects to use their certificates to move as soon as they want to, there will be a waiting list of residents who would like to move. They will be permitted to move on a schedule that will guarantee the development's cash flow. However, if a majority of the residents immediately express a desire to move, that will be a signal that the development is not providing good housing, and all residents will be permitted to move as soon as they want.

To promote 1) the development of mixed-income replacement housing in partnership with private investors, and 2) ownership by resident management corporations, a limited exception will exempt these projects from the requirement that certificates be family-based and portable. However, subsidies provided by the Housing Certificate Fund to the owners of such projects will be limited to the difference between the tenant contribution and operating costs and must not result in a subsidy above the market value of the housing.

Low-income use and demolition/disposition restrictions will continue to apply to the former public housing stock, as will protections for former public housing residents. Resident organizations and Resident Management Corporations will retain their right of first refusal when former public housing sites are sold. PHAs will be required to use the proceeds of any sales of former public housing for low-income housing purposes, including homeownership.

Transition Timetable

The goal for the transition from public housing to tenant based assistance is 3 years. This goal will be possible for those PHAs that have newer stock or have completed comprehensive modernization. Many larger PHAs, however, still have good developments with backlogged modernization needs. The following sets forth in detail the extended timetable for implementation. It permits a speedy transition to a market-based system for most public housing units, while providing flexibility to larger PHAs which may need additional time to improve their housing stock in order to compete in the market.

At each stage in this transition, the public housing system will be significantly improved from the current situation. For example, as soon as 1998 well over one-third of the public housing stock will be operating on the basis of rents determined by the competitive market value of the housing rather than on the basis of administratively determined Federal subsidies. By 1999, over one-third of current public housing residents will have real choice to live in housing that best suits their needs.

1995 Proposed statutory changes are enacted, permitting PHAs to demolish worst units and rehabilitate others in order to transition to market (Stage I).

1998 All PHAs with fewer than 100 units and at least one-third of the units in PHAs with more than 100 units move to project-based certificates with market rents (Stage II).

1999 The units that were project-based in 1998 become tenant-based (Stage III).

2000 All PHAs with 100-250 units and at least a second third of the remaining units move to project-based certificates with market rents.

2001 The units that were project-based in 2000 become tenant-based (Stage III). The remaining third of units in housing authorities with 250 or more units move to project-based certificates.

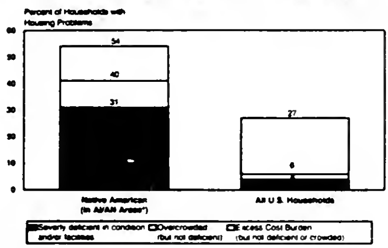
2002 *All* former public housing units are converted to tenant-based assistance (Stage III).

Minium Percent of Units With:	1998	1999	2000	2001	2002
Market-based rents	37%	37%	71%	100%	100%
Tenant-based subsidies	—	37%	37%	71%	100%

B. Native American Program Reform Consolidation

For many years Native American communities have been beneficiaries of Federal housing and community development programs. However, these programs have largely not been designed to meet the special needs and circumstances of Native American communities. Native American Tribes are sovereign nations that have a legal and political trust relationship with the Federal Government — a relationship that is very different from the relationship the Federal Government has with State and local governments.

Native Americans Face More Severe Housing Problems Than Other U.S. Households



* American Indian And Alaska Natives
Source: Urban Institute data and tabulation 1994

Native American housing conditions are some of the worst in America. Unemployment rates are very high and the economic opportunities are few. Native American communities are hampered in their ability to attract private capital in large measure because of a lack of a modern financial, legal and physical infrastructure.

While many larger Native American Nations take advantage of HUD's programs, the vast majority of them are smaller and lack the capacity to do so. The nature, timing and administration of these diverse programs inhibit comprehensive planning. In addition, under the current structure, most HUD programs are accessible to Native Americans only through competitions, making it difficult for smaller communities to successfully secure funding. Moreover, the lack of a predictable, steady stream of funding hampers rational and comprehensive planning. Finally, the current system for providing housing assistance to eligible low-income Native American families and individuals uses a variety of methods and a patchwork of programs that are difficult for both HUD and the Indian Housing Authorities (IHAs) to administer.

This proposal builds upon the reforms begun in 1993. Previously, Native American Nations had been required to deal with a whole series of individual programs which were administered by a number of different HUD offices. However, Native American programs were consolidated in one office, the Office of Native American Programs. The program consolidation allows the Department to better coordinate its Native American program activities, more effectively utilize its expertise on Native American issues and provide for better communication with the Nations on a variety of program issues. Furthermore, the direct oversight of the eight Native American Program field offices by the Office of Native American Programs in Headquarters contributes to a more direct relationship with the Nations in a government-to-government context.

Housing and Community Development Needs

This proposal further consolidates Native American programs and treats Native American programs separately, in order to address their housing and community development needs, while promoting self-governance and self-determination. This reform is based upon the expressed desires of Native American leaders and is designed to respond to their needs.

Native American governments, particularly smaller nations, have requested a consolidated formula funding mechanism with local flexibility. Therefore, funds will be set aside for Native Americans under the Affordable Housing Fund (AHF) and Community Opportunity Fund (COF) and these funds will be administered on a formula basis. Funds under both AHF and COF represent a significant increase from prior years, reflecting this Administration's desire to greatly increase available affordable housing and modern infrastructure.

The COF funds will represent an increase from 1 percent (under CDBG) in FY 1995 to 1.5 percent in FY 1996, or from $55 million to $122 million. The AHF funds will result in an increase in housing production funding for Native Americans from $14 million under HOME in FY 1995, to approximately $50 million under the AHF in FY 1996. COF funds will be available for all CDBG eligible activities. Native American communities will be able to use AHF funds for a broad range of eligible activities, including rehabilitation, new construction, acquisition, tenant-based rental assistance, first-time homeownership assistance, supportive services, service coordinators, and housing counseling. In addition, these funds will be available for activities such as the development of a legal/financial infrastructure, necessary to implement a modern housing and housing finance delivery system, and to fund a portion of other housing infrastructure (water and sewer).

The Secretary will be able to use 10 percent of AHF and COF funds to establish performance bonus pools.

Native American Nations will be eligible for homeless funding under the Homeless Assistance Fund (HAF). One and a half percent of the HAF will be made available to Native American Nations for developing and implementing continuum of care strategies to address homeless needs.

As with the other program consolidations, the cornerstone for identifying and addressing housing and community development needs will be set forth in a consolidated plan by each Native American Nation. The plan will contain the specific performance expectations the community hopes to achieve and performance will be measured against accomplishments derived from the plan. This is an excellent opportunity to increase the effectiveness of local decisionmaking and to promote long-term planning.

Homeownership

Native American governments have also requested assistance in developing both primary and secondary markets for mortgage financing. This proposal will continue the successful Loan Guarantee program which assists Native American homeowners in securing mortgage financing. The credit limit for this program was raised in FY 1996 allowing for additional single family loans to be guaranteed without requiring additional new funding.

This proposal also encourages the development of a Native American Finance Service Organization (proposed in legislation last year). NAFSO would provide technical assistance to Native American communities that wish to create Native American lending institutions, in order to provide primary mortgage lending as well as economic development lending. In addition, NAFSO would help to spur the creation of a secondary mortgage market by setting purchase goals for Fannie Mae and Freddie Mac. If these goals were not met, NAFSO would be authorized to engage in secondary mortgage activities.

Presently two-thirds of Native American housing units have been developed under the Mutual Help Homeownership Opportunity Program (MH), which is a lease-purchase program designed to enable low-income Native Americans to become homeowners. While future homeownership needs will be addressed through programs funded under the Native American set-aside under the AHF, the existing contract between the IHA and homebuyers will remain intact until conveyance. Project-based assistance will continue to be provided for those homebuyers who have not yet achieved homeownership potential on the amortization schedule for the unit.

Under the AHF, the ability for Nations to design their own specific homeownership programs will increase significantly. The uniform approach mandated by the Mutual Help Program has not allowed Native American Nations the necessary flexibility to address a wide-enough array of housing issues and environments. Under AHF, Nations will have the opportunity to develop specific programs which relate to their own cultural, social and geographic circumstances.

Furthermore, the AHF will permit the Nations and the IHAs to better leverage their Federal grant dollars which will produce additional housing for their members.

Rental Housing

While the Department's overall strategy for rental housing seeks to convert to a portable subsidy system, the nature of Native American housing markets and needs mandates a different approach. Unlike the rest of the United States, in Native American communities both low income and a severe lack of available housing prevail. In fact, the majority of Native American communities experience a shortage or total lack of private rental housing. In these markets a transition to tenant-based assistance will not increase housing choices for low-income Native American families unless they are willing to leave their reservations.

Therefore, some continued project-basing will be necessary. While the existing income eligibility to receive housing assistance under the Native American programs will remain at 80 percent of area median income in order to address unique circumstances such as physical remoteness of certain reservations from other non-reservation affordable housing, the Secretary will be authorized to give Native American governments, or their housing subsidiaries, flexibility to rent a specified portion of vacated units to anyone in need of housing, including those whose income will be sufficient to pay a true market-rate rent.

The most beneficial aspect of the proposal is to completely separate the Native American program from that of Public Housing. Historically, this separation has been completed only in certain areas and Native American Nations have had to cope with a variety of inapplicable or detrimental urban-oriented requirements.

Native American Housing Transformation

Program reform and consolidation will be accomplished in two stages:

Stage I: Deregulation and Program Consolidation

From Fiscal Year 1996 to 1998, Native American housing funds will remain project-based and will be allocated through an operating fund and a capital fund. Funds under the Affordable Housing Fund (AHF) and Community Opportunity Fund (COF) will also be available to federally recognized Native American Nations through a 1.5 percent set-aside under each of those funds. Native American communities will also receive a 1.5 percent portion of the technical assistance funds available under these funds. A 2-year period is necessary in order to give IHAs sufficient opportunity to transition to the Housing Certificate Fund (HCF). Those State-recognized Native American governments which have previously administered the Native American Housing Program in their jurisdictions will continue to operate the program as it is presently administered.

During this stage, the proposal will consolidate the existing maze of programs into a single capital fund and a single operating fund. The Capital Fund, which will be distributed to IHAs (except in certain circumstances) pursuant to a needs-based formula established by the Secretary, will consolidate the Native American Housing Development funds, modernization under either the Comprehensive Improvement Assistance Program (CIAP) or the Comprehensive Grant Program (CGP), demolition/disposition replacement housing, and technical assistance for resident groups and economic development and community service programs.

The following programs will be consolidated into the Operating Fund, to be distributed by a needs-based formula based on the current Performance Funding System, but modified to include the additional activities funded through this grant: Operating Subsidy (includes revised Allowable Expense Levels); Family Self-Sufficiency service coordinators, and the anti-crime/drug programs.

This proposal will repeal grievance procedures (rely on tribal law or, in very limited cases, State law); simplify program requirements for small IHAs; eliminate Federal preferences and implement Native American preferences; and re-target eligibility

All Native American housing authorities will be deregulated, but some IHAs will require more oversight based on a risk analysis model. Demolition/disposition/replacement housing requirements will be eliminated They simply do not address the housing environment of Native American communities and IHAs. The Secretary will also establish exceptions to the 1975 Education Assistance Act in order to allow greater discretion to meet Native American preference in contracting under certain circumstances.

In addition, in order to provide greater flexibility, ceiling rents at market conditions will be authorized. Finally, and most importantly, the Secretary will be authorized to make exceptions to the statutory requirements where individual circumstances warrant to promote the tenets of Native American Self-Governance. Native American Nations wish to increase their ability to determine their own direction. As a result, they increasingly need flexibility to design programs and processes without being constrained by Federal statutes. By allowing the Secretary to waive statutory provisions which are not consistent with an individual Nation's plans for self-determination and will not increase the cost to the Federal Government, HUD will be able to more appropriately respond to individual Nations.

Stage II: Implementation Phase

In Stage II, housing assistance will be market rate and project-based or tenant-based, depending on local needs For Mutual Help units, project-based assistance will continue to be provided until the homebuyer achieves homeownership potential.

During this stage, IHAs will receive a Housing Certificate for each Native American Housing Rental and Mutual Help Homeownership unit to provide for on-going operations and modernization activities. The IHA will receive a certificate on behalf of eligible families living in rental units and Mutual Help Homeownership units until the unit is conveyed to the homebuyer. The IHA will also be eligible to receive an appropriate share of incremental units. The amount of the assistance received by the IHA with respect to the Mutual Help unit will be based on the MH amortization schedule rather than the Fair-Market Rent which will be used for the rental program.

Native American communities will either retain their current housing authority or establish a new housing entity as administrator of the HCF funds. The community must develop a Consolidated Plan under which all housing activities will be coordinated.

The above applies to all federally recognized Native American Nations. Those state recognized Tribes which have previously administered the Native American Housing Program in their jurisdictions will receive housing certificates only for existing units, but will not receive incremental certificates or funding under AHF or COF.

At the end of this period, Native American housing and community programs will be funded the 1.5 percent allocations set-aside for Native Americans from the Affordable Housing Fund (AHF) and the Community Opportunity Fund (COF), 1.5 percent of the allocations set-aside for technical assistance under the AHF and the COF, and the allocations made available from the Housing Certificate Fund (HCF). In addition, the funding for new Native American housing construction which is being allocated through the Capital Fund will also be added to the AHF.

Of the total funds set aside for Native Americans under AHF and COF, 90 percent will be distributed on a formula basis and the remaining 10 percent will be distributed based upon performance. However, the Secretary will be authorized to fund smaller Native American communities that would otherwise receive de minimis annual funding based on the formula on a different basis. While AHF funds will primarily be used for housing and COF funds will primarily be used for community or economic development, in order to maximize the ability of Native American communities to address their particular needs and to promote the concept of self-governance, they will be permitted to use the entire amount of AHF funds for community or economic development purposes or the entire amount of COF funds for housing purposes. Transfers involving no more than 50 percent of the AHF or COF funds will be permissible without HUD approval. Transfers in excess of 50 percent will require HUD's consent.

Chapter Three: Federal Housing Administration

Across this Nation, millions of families need help in securing financing for one of life's necessities — decent, safe and affordable housing. For a number of reasons, including the lack of mortgage financing, achievement of the American dream of homeownership remains an elusive and unattainable goal for many families. Alternatively, the availability of affordable rental housing in many communities, particularly for lower income households, remains inadequate. There is also a continuing need for community hospitals and residential health care facilities.

For the past 60 years, the Federal Housing Administration (FHA) has played a critical role in addressing these unmet housing and health care facility needs, generating increased opportunity and renewed hope to millions of families. Through the efforts of FHA, 23 million households have been able to purchase a home, 4.5 million rental housing units have been produced, and more than 312,000 beds in community hospitals, nursing homes, and other assisted living facilities have been created.

Since the early 1930s, the Federal Government, and FHA in particular, have played a pivotal role in the complex system of mortgage finance. It is a role, as established in the National Housing Act of 1949, that recognizes the important, primary role that private enterprise must play in making mortgage financing available. But, the National Housing Act of 1949 also acknowledges the vital role that government assistance should play — that is, providing financing assistance to enable private enterprise to serve a much greater percentage of the total need. Today, the Federal Government's essential role as a catalyst — enhancing the availability of private mortgage credit to millions of Americans — remains the hallmark of FHA's success.

The Department's legislative proposal provides FHA with important tools for carrying out its catalyst role and for addressing our country's unmet housing and health care needs. The legislation contains two parts. First, the Department proposes to restructure FHA as a wholly-owned government corporation, called the Federal Housing Corporation. This new corporation, unlike the existing FHA, would function through consolidated, flexible product line authority and new operational flexibilities so that it can easily adapt to market demands and customer needs. Second, the Department is proposing several multifamily reform initiatives in the areas of portfolio restructuring, property disposition, preservation and enforcement. Taken together, these reforms will correct critical flaws in the way we have developed and managed our country's valuable stock of multifamily housing.

A. The New Federal Housing Corporation (FHC)

The Corporation's Role in Addressing Housing Needs

Young families, lower-income borrowers, minorities, residents of underserved urban and rural areas, and moderate-income families in high-cost areas all strive to make their modest wealth and income go far enough to purchase a home or to rent decent, affordable housing. Improvements in the ability of the private sector to serve these markets still leave millions of families, even families that have sufficient steady incomes to support a mortgage, unable to buy their own homes through conventional financing or to locate or afford decent rental housing units. Moreover, the Nation's principal supply of affordable rental housing is found in its older housing stock, often in smaller properties owned and managed by individuals or small businesses. The capital needs of this stock often exceed the private sector's current ability or willingness to participate.

Homeownership Needs: President Clinton recently charged HUD with developing an unprecedented public-private partnership to help a record number of families achieve the dream of homeownership by the year 2000. While the capacity of the private sector to serve a broader spectrum of housing needs is growing, many families continue to confront barriers to obtaining conventional financing. For example, under the new 3 percent downpayment initiatives of the private sector, many borrowers are, nevertheless, unable to afford the downpayment and closing costs usually required. These new high loan-to-value products require a 3 percent downpayment from the borrowers' own funds, an additional 2 percent down from other sources, payment of all closing costs in cash, and the set-aside of reserves equal to 2 full months of mortgage payments.

In contrast, FHA's underwriting guidelines permit greater debt-to-income ratios, allow the financing of more closing costs and premiums, and do not require any other set-aside of reserves. To achieve the President's goal,

FHA must both continue to serve those who cannot be served by the private sector, and work with its private and public sector partners in making homeownership a reality for many more Americans.

Rental Housing Needs: The vast majority of this Nation's poor families rent their homes. Rental housing shortages are severe and growing, especially for units affordable to the very poor. The United States went from a surplus of 400,000 affordable housing units in 1979 to a shortage of 4.1 million units in 1989. Recently, other than the modest production resulting from use of the Low Income Housing Tax Credit, there has been little new affordable multifamily housing development.

The private credit markets fail to serve this rental submarket adequately. Multifamily loans lack standardization, they often require multiple layers of subsidy and financing and complex "one of a kind" solutions. Capital is not consistently available, particularly for smaller loans on small properties. FHA's credit enhancement has historically and should in the future bring lenders and private investors to markets they would otherwise not serve.

Health Care Facility Needs: Community hospitals, nursing homes and other health care facilities are a vital element of vibrant neighborhoods and communities. Many of our Nation's urban and rural hospitals, as well as other health care facilities, suffer from obsolete and inefficient facilities, exacerbated by their inability to attract private lenders to finance capital projects.

Although the construction and modernization of health care facilities is expected to grow at an annual rate of 5 percent during the next several years, private lenders are often reluctant, without Federal credit enhancement, to provide financing for the development of these facilities, especially those located in older inner-cities and rural communities. These facilities bring benefits to their communities by creating jobs, stabilizing neighborhoods, and improving the quality of life through enhanced health care accessibility.

FHA's Unique Role in Providing Access to Credit

FHA benefits the underserved: For years, FHA has made home purchase possible for working Americans, members of minority groups, and immigrants struggling to provide a decent home for their families. FHA especially serves first-time homebuyers, who have had the least opportunity to accumulate the wealth and income necessary for home purchase. Additionally, FHA has played a pivotal role in the financing of affordable rental housing units. FHA's success in serving the underserved is illustrated as follows:

- In 1993, over 69 percent of FHA home purchase loans in metropolitan areas had low downpayments (less than 5 percent down) compared to 1/10 of one percent of loans purchased by the GSEs. Two-thirds of FHA's single-family business benefits first-time homebuyers, while only 30 percent of conventional loans (within FHA's mortgage limits) serve first-time homebuyers. 47 percent of FHA mortgages were for homes under $70,000 compared to less than 22 percent of privately insured mortgages.

- While FHA accounts for 23 percent of all home purchase loans in metropolitan areas, it accounts for almost 45 percent of the loans going to Blacks and Hispanics. In fact, FHA insures twice as many loans to African Americans as all private mortgage insurers combined.

- In 1993, almost 30 percent of FHA loans benefitted underserved areas (census tracts with either low-income or high-minority composition), while only 15 percent of conventional loans benefitted these areas.

- For families who either choose to rent or who are unable to purchase a home, FHA plays a major role in financing multifamily rental housing. Currently, there are two million privately owned and managed rental units financed with FHA-insured mortgages; 1.6 million of these units are affordable and benefit from an interest rate or rental subsidy.

The Federal Government can play a critical role where the private sector cannot: The Federal Government has certain inherent advantages — most importantly a lower cost of capital — that reduce its cost of doing business below that of the private sector. Compared to private mortgage insurers, the Federal Government borrows funds less expensively, must set aside fewer reserves, pays no taxes, and has no duty to return a profit to its private shareholders. This lower cost of doing business will allow the Federal Government to insure loans on a self-sustaining basis that would be unprofitable for the private sector to insure.

FHA has historically, and will in the future, play the following four pivotal roles:

- **Expanding access to capital to borrowers who otherwise would not be served.**

- **Pioneering and standardizing new mortgage products. For example, FHA pioneered the 30-year fixed rate home mortgage, which became an industry norm.**

- **Providing stability to mortgage markets during economic downturns.** For example, during the 1980s in the oil-patch States, the percentage of loans insured by PMIs plummeted, exacerbating local economic problems. In contrast, FHA continued to make mortgage credit available, moderating the severity of the downturn.

- **Standardizing housing and health care facility credit delivery.** For example, FHA has filled gaps in the credit delivery system supporting the development of affordable rental housing and health care facilities in distressed communities.

The Need for Reinvention of Today's FHA

Notwithstanding FHA's historic accomplishments, as the private housing finance market became sophisticated during the past decade, FHA failed to keep pace. Today's FHA is outdated, inefficient, and increasingly ill-equipped to prudently manage a Fortune 100-sized insurance company with a $380 billion portfolio of insurance-in-force backed by the U.S. taxpayer.

Specifically, FHA cannot respond to changing market conditions, because its products and operations (including personnel and procurement practices) are prescribed by legislation and further constrained by appropriations. FHA lacks the technology it needs, even when technology acquisition would produce savings. FHA is precluded from acquiring outside expertise quickly; for example, it took FHA 11 months to hire a financial advisor in connection with multifamily note sales. During that time interest rates rose. As a result, sales proceeds were diminished and FHA's ability to recoup savings in the insurance fund was reduced.

Structure, Governance, and Powers

This proposal builds on the need for a continued Federal role in the mortgage credit markets, while avoiding the bureaucratic inefficiencies that hamper the current structure and prevent FHA from reaching its potential. By creating a new government-owned Federal Housing Corporation (FHC), FHA will be transformed into a streamlined, business-oriented government entity that can operate efficiently, while being held accountable for accomplishing its public purposes in a safe and sound manner.

The Government Corporation Control Act (GCCA) contemplates that certain government functions of a business-like nature will be carried out from within a corporate structure. This proposal, using the GCCA model, and subject to all the provisions of the GCCA, structures the FHC as a wholly owned government corporation under the oversight and direction of the Secretary of HUD. The new FHC will be a self-sustaining financial institution with clear accountability for performance and results. The FHC's safety and soundness will be monitored by the Office of Federal Housing Enterprise Oversight (as is the safety and soundness of the privately owned GSEs), while its programmatic operations and performance of its mission would be implemented and coordinated with national housing policy by the Secretary of HUD.

While the structure and efficiency of today's FHA will be significantly improved through the FHC, its fundamental purpose — to facilitate homeownership and affordable rental housing opportunities, and to address unmet housing and health care facility mortgage credit needs — will not change. The current FHA's numerous statutory insurance programs will be consolidated and simplified into a few broad, flexible authorities directed to general market sectors: single-family and home-ownership, multifamily and rental, and health care facilities. This consolidation will enable the FHC to effectively respond to changing market demands and conditions. For example, if a particular product line is not effective, the FHC, unlike today's FHA, will be able to quickly modify or terminate the product.

The corporate powers of the FHC will be vested in a Chief Executive Officer, appointed by the President, with the advice and consent of the Senate. The Secretary will be authorized to appoint an advisory board to obtain guidance on the operation of the mortgage markets, the housing credit needs of vulnerable populations and communities, and any changes needed to carry out the FHC's public purpose mission.

The FHC will be authorized to provide credit enhancement, engage in related asset management and disposition, and provide credit-enhancement related services, products and information. FHC's obligations will have the same U.S. Government backing as do FHA obligations today. Moreover, to ensure that the FHC does not inappropriately interfere with private market activity, the FHC will be subject to two general limitations upon its business: (1) a maximum mortgage amount, which will be set and adjusted at the FHA's current statutorily imposed limit; and (2) a 5-year aggregate new business limitation.

The FHC will continue its historic pioneering role, expanding the reach of the private sector into markets not traditionally served, through its traditional mortgage insurance products and risk-sharing. Today, FHA possesses demonstration authority to enter into risk-sharing agreements with private and other public partners in the multifamily arena, under which FHA shares the risk of mortgage default with other well-

capitalized public and private institutions. Properly designed, risk-sharing matches the benefits of Federal credit enhancement with the capacity, technology, and entrepreneurship of the private sector partner. This arrangement promotes efficiency and provides the taxpayer with further protection against losses.

Mechanisms Ensuring Accountability

In exchange for flexibility in its operations, administration, and lines of business, the FHC will be held accountable through established performance measures and other oversight mechanisms. The Secretary will establish a series of public purpose performance requirements for each year's activities. The requirements will ensure that a specified proportion of the FHC's business benefits vulnerable populations, families, communities, and markets underserved by the private mortgage markets.

The FHC will also be subject to financial safety and soundness performance requirements, designed to ensure that the FHC is capable of covering not only anticipated expenses and liabilities but also protecting the taxpayer against unanticipated losses. The Director of the Office of Federal Housing Enterprise Oversight (OFHEO) will be the safety and soundness regulator and develop a risk-based capital adequacy model to ensure that the FHC continues to operate on a self-sustaining basis. OFHEO will have the authority to take appropriate enforcement action if the FHC fails to operate in a safe and sound manner. OFHEO's estimates of performance will serve as the basis for the credit subsidy cost estimates to be reflected in the President's budget. Additionally, the FHC will be subject to an annual audit, performed by a qualified independent third party, and to the oversight of the HUD Inspector General.

Operations

The FHC will be granted flexibility in its personnel and procurement practices, in order to more effectively respond to changing conditions. Notwithstanding this flexibility, the FHC's practices will continue to reflect the principles embodied in the Federal Property and Administrative Services Act and the Civil Service laws. The FHC will be authorized to establish salary schedules that mirror those used by Federal banking regulatory agencies.

Treatment of Existing Portfolio

The operational flexibility and business-like incentive structure of the new corporation will provide an opportunity, not only to manage new business more effectively, but also to reduce the government's potential exposure on FHA's outstanding portfolios. For both budgetary and legal reasons, the new business and the inherited business of the new FHC will be segregated into different insurance funds. While the new funds will operate under the requirement of overall self-sufficiency, the existing obligations will retain their existing budgetary treatment.

Transition Period

To accommodate initial start-up, the FHC charter will identify a transition period that will commence upon the FHC's date of incorporation. During the transition period, the FHC will invest in new capital systems and infrastructure, develop rules and guidelines governing the FHC's new business products and operations, and phase out operations under existing insurance authorities. It will also continue to issue mortgage insurance in connection with ongoing operations of existing FHA programs, until the newly authorized products and funds are sufficiently under way.

Also during this period, the FHC will be authorized to undertake new business under the authorities set forth in the charter. Once it is fully operating as a going concern, the FHC would cease executing new business under pre-existing insurance funds.

Ginnie Mae

The Government National Mortgage Association ("Ginnie Mae") will continue to guarantee securities backed by pools of mortgages fully insured under the National Housing Act, including those to be insured by the Federal Housing Corporation.

The Ginnie Mae charter will be amended in two manners to reflect changes being made in the Federal Housing Corporation Charter: 1) to permit the excess of revenues over both expenses and provisions for losses to be transferred to the MMI fund to ensure that the MMI fund meets statutorily required capital standards; and 2) to mirror the Federal rulemaking, procurement, and personnel policies applicable to the FHC.

Additionally, the Treasury Department, Ginnie Mae, the Federal Housing Administration, and the Office of Management and Budget are currently studying the impact of having Ginnie Mae participate in risk-sharing arrangements between the Federal Housing Corporation and various private and other public entities. The result of this study will determine whether any additional changes to Ginnie Mae's charter are necessary.

B. Multifamily Portfolio Management Reforms

The Federal Housing Administration (FHA) has operated rental housing programs for almost 60 years to help low-income Americans find affordable rental housing. In seeking to meet this national objective, FHA and HUD have designed and operated several dozen development and/or subsidy programs since the late 1950's, insuring mortgages over this period that resulted in the production of more than 4.5 million rental units.

The current FHA portfolio contains approximately 2 million privately owned and managed rental units of which approximately 1.6 million also benefit from mortgage and/or rental subsidies provided by HUD (the assisted stock). About 87 percent of all tenants in FHA-insured properties are low-income renters with incomes below 80 percent of median and, of that, over 50 percent have incomes well below 50 percent of median income. Elderly and disabled household occupy 19 percent of the unassisted stock and almost half of the assisted stock.

Beginning in the mid-1960's and up until 1982, the FHA operated no less than twelve different combinations of mortgage insurance, direct loans, and subsidy programs. Most of these programs have been closed for over a decade but the buildings, tenants, legal contracts, costs, and neighborhoods remain a part of the current and future responsibility of this Department. The original intent of these programs was to serve low- and moderate-income renters, stimulate the economy and produce jobs, stimulate investment in real estate by passive investors through tax shelters, and, of course, to produce new privately owned and operated rental housing scattered throughout the country. The majority of these units remain both subsidized and insured today serving very low and low-income tenants ranging from elderly couples in the New Jersey suburbs, to working mothers in Northern Virginia, to disabled residents living and working in small communities.

Unfortunately, many of these programs were flawed in their basic design and/or operation. This does not mean that the real estate is deficient; in fact, the majority is well maintained and critical to the 1.6 million households who live there. HUD has identified flaws which can be corrected: poorly trained and overworked staff; lack of sufficient data for more than 17,000 properties and/or mortgages, many of which nothing was known about; a large portfolio of foreclosed properties and HUD-owned mortgages; a lack of commitment to and knowledge of enforcement tools; a substantial number of over-subsidized projects; legal contracts which prevented proactive solutions; systems which discouraged enforcement due to the "perceived cost of foreclosure"; landlords who were burdened with preference rules and lacked incentives to invest; and tenants trapped in poor living conditions.

The most serious flaw is that the government and the residents are trapped in a difficult, no-win situation because the subsidies pay the debt which is insured by FHA. If HUD/FHA lowers the rents or enforces the rules on maintaining property standards, FHA ends up paying a claim against the GI/SRI insurance fund and eventually owning the real estate through foreclosure.

Other critical flaws are a) owners are not and were not rewarded for the return on their investment or the quality of the real estate; instead, they are rewarded through tax incentives, management fees and payments for services, b) for much of the stock rents are significantly above market because HUD paid for the initial costs of development by raising rents above market and per law has continued to raise rents regularly since, c) in other stock, without deep subsidy where HUD sets the rents, the rents are often below market because HUD is reluctant to allow increases in tenant payments; this results in properties falling into disrepair because of insufficient rental income, and d) owners are overburdened with regulations and reporting requirements but are not measured actively on the quality of their real estate.

To make matters more difficult, as real estate began to show the effects of these problems as early as 1980, HUD's response was to ignore the problem, fix the effects but not address the cause, or blame it on "bad owners." This situation was first identified in early January 1993. However, the degree of the problem is only now being fully understood by the larger housing and legislative community. Many of the current problems are not a result of flawed design, but of the equally destructive neglect or quick fixes which were allowed or encouraged by having laws, policies, and regulations of the last 15 years.

In the 1980s, HUD multifamily program resources declined, while workload demands increased. The investment in technology, systems, and training was sporadic. Limited travel resources prevented staff from visiting troubled properties. Finally, staff were directed not to force a mortgage into default by enforcing property condition standards, because it would cost FHA money to pay claims.

To compound this untenable situation, the economy got worse in the late 1980's, increasing the rate of unavoidable foreclosures. Programs such as the poorly designed and managed Coinsurance program added to the portfolio. As a result, the Department held over 2,500 mortgages when this Administration arrived in 1993. And, because few dollars were appropriated for property disposition, the sale of HUD-owned properties had come virtually to a halt.

Finally, HUD and Congress must now face the Section 8 contracts for this inventory, an estimated $64 billion over the remaining mortgage terms and in addition, the costs of current property disposition and, preservation programs which are substantial.

Initial Actions to Address Problems

HUD has implemented systemic solutions which are an important foundation for the more radical change which is proposed.

The Department made it clear that it was not afraid to foreclose or enforce standards for good housing. Since 1993, HUD has *increased* foreclosure actions or other enforcement efforts several times over. Actions include changing management agents in over 400 instances, abating (cancelling) the Section 8 on 65 projects (compared to only three abatements in the previous years), and selling several hundred mortgages and seven times as many properties in 1994 as in 1992.

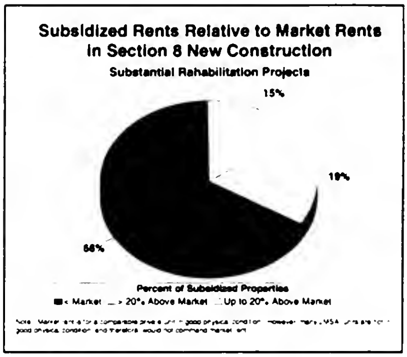
HUD proposed reforms to the Property Disposition program which were signed into law in April 1994 and which have already reduced potential property disposition costs by several hundred million dollars.

The Department began staff training jointly with industry groups, set up the first early warning system for the portfolio, collected and reviewed 95 percent of the required financial statement information on the portfolio (50 percent more than in 1992), and reduced the GI/SRI loan loss reserve by over a billion dollars.

Thus, HUD identified the problems and began several initiatives to address the problems. However, it is clear that a more radical change is required to end excessive subsidies, stop significant stock deterioration, and relieve both owners and tenants of the massive burden imposed when rules replace common sense. This proposal, which comprises several initiatives in the areas of portfolio management and enforcement, preservation, and property disposition, will achieve this result.

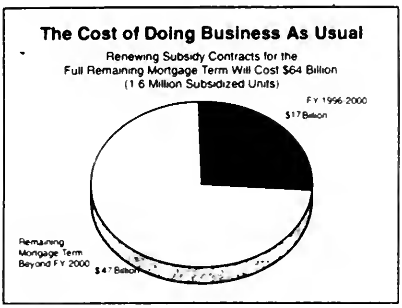
The Need for Portfolio Restructuring: Mark-to-Market

Mark-to-Market addresses the most critical flaw — the interdependence of subsidies, debt payments and insurance. By separating the subsidies and insurance, we can reduce costs, provide residence choice, insure real estate based incentives to owners, and improve the quality of the housing. Currently, three-fourths of the inventory of 4,100 insured Section 8 new construction and substantial rehabilitation (NC/SR) properties have rents in excess of the local Fair Market Rents (FMR), and two-thirds of these properties have rents more than 20 percent over the local FMR. These projects, containing 360,000 units, receive automatic increases in rents whether the property is run efficiently or not, and regardless of whether the rents are market competitive.



As many as 3,000 properties of our older assisted properties that pre-date the Section 8 NC/SR program, lack the necessary resources to be maintained as quality, affordable housing. The condition of this inventory of 330,000 units ranges from moving in the direction of "economic obsolescence" to already deeply distressed. The traditional approach has been to add project-based Section 8 funds or Flexible Subsidy to bolster rental income, fill vacancies, replenish depleted replacement reserves, and make physical repairs. Sometimes these short-term fixes have worked, but often they only postponed default.

It will cost the Federal Government $17 billion to renew the project-based Section 8 contracts that will expire between FY 1996 and FY 2000 to cover the remaining term of their mortgages. The cost jumps to $64 billion to renew subsidies for the 1.6 million units of project-based



Section 8 which expire between now and the year 2020. Renewing contracts without restructuring maintains oversubsidizing, sheltering owners from the market competition and limiting tenant choices *It is also the most expensive course.*

Overview of Multifamily Portfolio Reforms

The multifamily reforms are based on the premise that it is better and less expensive to pay a claim earlier (full or partial) than continue propping up projects with higher or additional subsidies or to pay a claim and then bear the cost of foreclosure and disposition. The reform effort also comprises several initiatives in the areas of portfolio management and overlapping changes in enforcement, preservation, and property disposition.

Separating future Section 8 renewals from the property provides for a new legal and financial relationship with owners at contract expiration and adjust the value of the real estate to market. The real market value of the real estate is recognized through adjusting the debt level. Future incentives and benefits of real estate ownership will be based on good management and investment in the real estate going forward, and not subsidies from the Government.

Tenants will be free to choose where they live (including living in their current home in the majority of cases), and retain subsidy support on a resident basis. FHA will be provided the tools to maintain an active and viable mortgage portfolio. These include the ability to accept partial payment of claims and restructure existing debt when the real estate value is below existing debt without taking full assignment of the loan. Existing tools will be expanded such as selling mortgages and foreclosing quickly where necessary and then disposing of properties more cost-effectively. Also, FHA will again be in a position to enforce with vigor.

New partnerships will emerge with both existing and new investors and lenders. The real estate community will be asked to play both traditional servicing roles and new roles as investors in both debt and equity. FHA will rely heavily on each group to assist in executing much of the specific activities of the planned restructuring.

It is expected that properties which are both insured by FHA and subsidized by HUD will break down into three basic groups. (1) those which after the subsidy contract expires require no further assistance, except individual tenant-based resident subsidy when the tenant is eligible, (2) those which will require the restructuring of the mortgage, a short-term contract renewal on a project basis and modification of other aspects of their prior legal obligation, and (3) a small but notable segment of the stock which cannot work (rents don't even pay expenses) even if the Government forgoes debt. These properties will require a change in the real estate including a new unit mix and/or ownership, external support, or even partial or complete demolition. Again, residents will be provided individual tenant-based assistance.

The following briefly outlines for potential outcomes each of the three categories of properties in more detail. Since, as was discussed at the outset, there are well over a dozen different prior programs and sets of rules which will require changes, this presentation covers the major outcomes and categories only.

No Claim Payments/Prepayments. It is expected that approximately 25 percent of the assisted portfolio encompasses projects with owners who will elect not to renew the subsidy and to repay or refinance the mortgage at no additional cost to the Government.

The only cost to the Government will be the cost of conversion to tenant-based subsidies. Rents may exceed FMR over time and tenants will need to move. Current requirements for tenant notification will continue to be applied. It is not expected that the tenancy changes will result in massive tenant relocation but some relocation will certainly occur, especially over time. Certificates will be available to eligible households from the Housing Certificate Fund.

In some cases, the property owner will seek refinancing from FHA through 223(a)(7). Any cost would be that of a new loan as described in other parts of the existing FHA budget.

Partial Claims. Most properties will be allowed to restructure their debt before, or at the time, the contract for Section 8 expires.

The majority of projects will be unable to pay current debt service and operating costs when the rents are reduced to market. These projects are good, solid, affordable housing, but must see a recognition of real current value in the debt levels to survive separating the subsidy without causing a full mortgage default and then foreclosure.

Today, the Department can adjust the loan amount and pay a partial claim to the investor/lender as a workout. The owner retains the amount as nonamortizing debt, in most cases as a second mortgage. The Department is now proposing to offer this to borrowers at or prior to contract expiration. To the extent it can be done voluntarily by owners, lenders and investors today under current authority, this will be done. However, the current authority is very limiting and does not provide for recapitalization unless HUD pays a full claim and takes control of the real estate. Further, it does not allow the Department to allow the mortgagee to put the mortgage to the Department for restructuring without paying a full claim. The latter mechanism will require legislation. It may also be advantageous to encourage borrowers to voluntarily restructure prior to contract expiration. This will require additional legislative authority.

In all cases, eligible residents will be provided with short-term (up to 2 years) project-based protection. Elderly and disabled households may at their option retain the project-based subsidy as long as they are eligible and funds are appropriated to the Housing Certificate Fund. Other households will receive certificates at the end of the transition period, so long as they are eligible. They may use them in place or move if they choose. Owners with restructured mortgages will be required to accept voucher or certificate holders.

Full Claims (with foreclosure). Some properties are not now nor can they be made economically or socially viable simply by restructuring. In this situation, restructuring means foreclosing on properties and providing tenants with certificates to seek other housing. These properties will then be disposed of as outlined in the property disposition section.

Implementation of Portfolio Restructuring

To implement this portfolio restructuring, HUD must acquire staff and contractor expertise. HUD also cannot abrogate existing subsidy contracts. HUD is therefore planning for a phased-in approach starting immediately and extending over the term of the majority of the contracts. This will allow time to build internal and partner (contractor) expertise. The RTC, FDIC, and their private sector contractors have demonstrated that Mark-to-Market can be successfully applied to restructuring large real estate portfolios. The Department intends to use the expertise of intermediaries and to build on its success in mortgage sales. Strategies will include the establishment of structures like the RTC/N series which allow third parties to complete the workouts and the HUD-G4 auctions which enable the market to effectively evaluate and restructure debt.

Please note that the alternative to Mark-to-Market, abrogation of existing contracts, is also staff intensive, complex, and expensive. The resulting foreclosure and property disposition for the majority of the stock is the most expensive alternative and requires longer timeframes, and abrogation will most certainly result in litigation. This option at first appears attractive because properties are immediately exposed to a market-based determination of their rents. But no renewal will also trigger disinvest-ment and massive defaults. A planned restructuring allows for market determination without disinvestment and default.

For properties sold in FY 1994, it often took over 2 to 3 years for HUD to sell a project after it acquired title. During this time, HUD has the staff-intensive responsibilities of managing, repairing, and marketing the property. This does not include the several years it can take to move from paying a claim to going through foreclosure to acquire title which often involves lengthy bankruptcy proceedings and further disinvestment.

The costs of disposition are also high. Currently, the net per unit cost of an insurance claim for Section 8 NC/SR is $35,000 and about $17,000 per unit in other assisted properties.

Mark-to-Market is the alternative that offers the prospect of fewer defaults and is less costly and disruptive. Partial claim payments are estimated for Section 8 NC/SR units and for units in other assisted properties. Assuming no repayment of the deferred loan, the partial payment costs less than a full claim— $17,300 on a typical Section 8 NC/SR unit and $7,300 per unit for other assisted properties.

Reform of Property Disposition

The Multifamily Property Disposition Reform Act of 1994 (Reform Act) made a number of program improvements that increased HUD's ability to deal efficiently with sales of foreclosed or HUD-owned property and provided the Department with some necessary tools for sales to nonprofit entities and resident organizations. Further program reforms are needed now, both to conform our practices and policies in property disposition with the proposed operating procedures for the new, entrepre-

neurial FHA and to address the budget realities that make a more cost-efficient approach essential in any future scenario.

The Department is proposing legislative changes to achieve these goals:

- Protect residents when properties are caught in the default/foreclosure/sales cycle;
- Prevent properties from becoming or continuing to be a blight on the communities where they are located, and instead manage and sell the properties in a way that will contribute to neighborhood preservation or revitalization;
- Provide consistency in the Property Disposition program with the Mark-to-Market proposal, particularly with regard to delinking of subsidies from real estate; and
- Achieve further cost savings by procedural changes that would improve the sales process and reduce HUD holding costs.

Funding for new Property Disposition assistance would be provided as part of the Housing Resolution Fund, which will be included in the mandatory budget as part of the FHA GI/SRI liquidating account.

The proposed property disposition reforms listed below cover both substantive and procedural areas.

Program Goals. The existing statute lists goals for the property disposition program which address preservation of affordability, maintenance of stock, preservation and revitalization of neighborhoods, minimizing displacement and demolition, and supporting fair housing strategies.

HUD proposes to amend the goals, authorizing the Secretary to ensure that the program can be administered in a way that is consistent with the principles underlying the restructuring of the FHA portfolio and those of the proposed new corporate FHC. New goals will minimize the cost to HUD of the foreclosure and HUD-owned sales process, encourage partnerships in the disposition of HUD-owned properties, and provide broader flexibility in management and sales practices designed to allow balance among competing goals.

Resident Protections. Residents of foreclosed properties held by HUD are currently protected at the time of sale in a number of ways. Assistance may come through project-based Section 8 rental assistance for up to 15 years, by long-term affordability restrictions; or by protecting very low income residents from rent increases for 2 years after sale of the property.

HUD now proposes that HUD-owned properties be treated consistently with insured properties going through the Mark-to-Market process.

For subsidized properties, this will mean that up to 2 years of project-based rental assistance will be provided, funded through the Housing Resolution Fund in the mandatory GI/SRI account. After this 2-year transition period, families residing in units with project-based certificates will receive a portable subsidy, which could be used to continue to rent in the property or to move to another property of the family's choice.

Elderly or disabled households will be offered an option as in restructured properties to retain the project-based character of the subsidy so long as the tenant is eligible and the unit rent is eligible under the rules of the Housing Certificate Fund. They could alternatively choose to receive a portable subsidy.

For families in unsubsidized properties (i.e., those with less than 50 percent of the units under a project-based assistance contract) that had been receiving other types of project-based, deep rental subsidy, such as rent supplement or rental assistance payments, or loan management set-asides, housing certificates will be provided.

Very low income tenants in unsubsidized properties who are not receiving assistance will be directed to the Housing Certificate Fund.

Preventing Blight. Under the current law, HUD can use up-front grants to pay for repairs to properties that it has determined should be preserved as affordable rental housing. These grants will continue to be part of the Housing Resolution Fund.

Consistency with Mark-to-Market. Consistent with the movement to tenant-based assistance to bring the portfolio into a market-based economy, the definitions of affordable units now mandated in the statute should be deleted. The current definition for unsubsidized units is based on the relationship of rents to income levels of the occupants — i.e., no more than 30 percent of the applicable income limits of 80 percent of the area median income for low income and 50 percent of the area median income for very low income.

These changes will make foreclosures and HUD-owned sales generally consistent with the Mark-to-Market approach, sales will be structured to capture the true market value of the property, which in many cases will be higher than the use-restricted value. Freeing subsidies from properties effectively ends the need for post-sale use restrictions.

Streamlining the Sales Process. Several proposals relate to streamlining the sales process and reducing holding costs.

The Department is committed to building partnerships with State and local governments and encourages their purchase of HUD-owned properties particularly for transfer to resident ownership or community-based nonprofits. However, to avoid excessive holding costs, the current right of first refusal must be simplified and streamlined, to provide a time-limited window in which State and local jurisdictions could notify HUD if they want to negotiate a purchase. Governmental bodies will continue to be invited to comment, and to offer recommendations on disposition of specific properties within their jurisdictions, when they chose not to negotiate a purchase.

Finally, the Department is recommending a series of smaller amendments designed to streamline the property disposition program by eradicating detailed program and reporting requirements governing the most routine operations, such as how to select a buyer, contents of the disposition plan, how owners should contract for property management, and like activities. These must be deleted. In addition, burdensome reporting requirements, which hamper the Department's asset management efforts, must also be eliminated.

Two other proposals address foreclosure issues in other laws. The first is to remove provisions of the Multifamily Mortgage Foreclosure Act that require purchasers of residential properties sold at foreclosure to maintain any long-term use restrictions that the original mortgage insurance imposed on the property.

Finally, exemption of multifamily housing from the automatic stay provisions of the bankruptcy code is needed. Under current law, owners who file for protection can prevent HUD from foreclosing and taking possession of the property quickly. This exemption will protect the interests of both the tenants and HUD by permitting foreclosure to proceed with minimal delay.

Preservation Reforms

In 1990, Congress acted to preserve the long-term affordability of older assisted stock. This action was the last major modification to the programs discussed at the beginning of this chapter. The Preservation program paid owners accumulated equity through increased rents to existing or new owners. Again, the FHA fund financed this oversubsidization. Since this is an ongoing program, FHA is proposing a blend of reforms which incorporate restructuring while maintaining legal commitments.

To encourage the development of lower income housing during the late 1960's and early 1970's, mortgages with 40-year loan terms were insured by FHA under Section 236 and 221(d)(3) programs. Certain of these mortgages allowed the owner to prepay the loan without HUD's consent at the end of 20 years. In 1987, with the 20-year anniversaries approaching, Congress imposed a moratorium on the ability of owners to prepay, in order to develop a mechanism to encourage owners to preserve this housing as affordable to low and moderate income families for at least the remaining term of the mortgage.

Congress passed the Emergency Low Income Housing Preservation Act of 1987 (ELIHPA) and then the Low Income Housing Preservation and Resident Homeownership Act of 1990 (LIHPRHA). These programs offer generous incentives to owners to continue to operate the properties as low-income housing. The highest and best use of many of these properties is low-income housing, and given the opportunity to prepay, it is anticipated that only 25 to 30 percent will in fact do so in today's market environment.

LIHPRHA also establishes a hierarchy of priority purchasers for owners who wish to sell and provides technical assistance and development grants to assist residents to play a major role in preservation planning or to facilitate acquisition of the property by residents or community-based nonprofit organizations.

Problem. Preservation relies on incentives to encourage owners to retain the housing for low-income residents; the program offers long-term project-based rental assistance contracts at rents that can exceed the FMRs, and values properties at their highest and best use through a complex appraisal process. Preservation has been achieved at very high cost to the Government (there have been about 50,000 units in 200 properties completed since the enactment of ELIHPA in 1987 with costs in excess of $17,500 per unit) and with excessive administrative burdens on participants and the Department.

Currently, many of the provisions of the two programs contradict the principles of HUD reinvention and of FHA restructuring. They emphasize continued long-term linkage of subsidies with real estate, artificially imposed above-market rent structures as opposed to market-

driven rents, and bureaucratic, complex requirements which fall on private owners, residents, and units of State and local governments.

The Department proposes to reform LIHPRHA into a new program (New Preservation) that is less expensive and more realistic operationally. Resident empowerment will continue to be supported with technical assistance grants. The New Preservation program will continue to provide acquisition assistance for the preserved property, but only for acquisition by qualified resident organizations or other community-based nonprofits.

Only those properties with low rents and significant equity demonstrated by an appraisal submitted before February 6, 1995, will be eligible to participate in the new program. Properties which do not participate in the new preservation program will either remain as affordable housing under their current ownership, or the mortgages will be prepaid and the properties become subject to market disciplines which mandate owners to operate them at competitive prices in order to remain viable.

This proposal is designed to achieve the goals of resident organizing and capacity-building, provide protection for residents (including tenant-based assistance for properties where mortgages have been prepaid), encourage non-profit ownership of properties which are sold (to encourage community-based and community-responsive owners), and community stabilization by allowing properties to find their market niche through repayment or sale.

In order to transition to the new program in an orderly manner, any project owner who obtained plan of action approval by February 6, 1995, the transmittal date of the President's FY 1996 Federal Budget, will be "grand-fathered" under LIHPRHA. All other owners otherwise eligible for LIHPRHA will either qualify for preservation benefits under the new program or have the option (but not the obligation) to prepay the mortgage.

The new program is a significant departure from current practice. First, the program will be voluntary. Every owner will have the right to prepay at any time without HUD's consent after the 20th anniversary of the mortgage. If a notice to sell, or to extend the use as affordable housing and receive incentives, has been filed (but the transaction has not closed), owners could change their minds. Owners meeting the eligibility requirements will have the option to participate in the program by selling to a nonprofit purchaser.

Second, properties with approved Title VI Plans of Action (i.e., whose use agreements have been executed pursuant to an approved POA) and Title II projects that have Preliminary Approval of Plans of Action on the "grandfathered" date will continue to be processed under the original Title VI program.

Third, properties eligible to participate in the program will be those with an appraisal submitted by February 6, 1995, showing a minimum equity of $10,000 per unit and rents no higher than HUD's Fair Market Rents or the "street rents," if less. Disagreements concerning equity will be resolved by HUD based on a capitalization rate applied to a market-driven net operating income, taking into consideration rehabilitation needs, replacement reserves, and comparable rents.

Fourth, sales price to the nonprofit will be based on market value as negotiated between seller and purchaser. FHA will retain authority to insure mortgages on preservation properties. Debt represented by the first mortgage could be deferred. To effect this, HUD will have the ability to accept assignment without penalty to the seller or buyer. Low-income use restrictions of the first mortgage will remain in place.

Finally, Preservation Technical Assistance Grants for non-profit purchasers and the current "Shallow Rent Subsidy" for low-income residents receiving Section 8 subsidies will be retained. Nonprofit purchasers will be permitted a 6 percent, surplus cash, return on invested capital.

Properties not eligible for preservation benefits will be handled under the following rules. Properties with approved Plans of Action that continue processing under the original program rules will be offered nonrenewable 5-year contracts for project-based Section 8 rental assistance. At the expiration of the 5-year contract, eligible residents will receive subsidy under the Housing Certificate Fund which they may use to continue residing in the property or to move to another property of their choice.

Residents of properties with project-based Section 8 contracts where the mortgage is prepaid will be offered a portable subsidy from the Housing Certificates Fund when current contracts expire.

Other Enforcement Reforms

Similarly, the Department proposes other enforcement and technical remedies. Broadened enforcement authority is necessary to expand the use of civil money penalties against owners and certain managing agents who violate regulatory agreements or Section 8 HAP contracts, equity skimming provisions to all insured programs and Section 202, doubled-damage penalties and penalties for obstructing a Federal audit, as well as to authorize the mortgagee review board to immediately suspend mortgagees that violate HUD rules.

In order to save significant unnecessary subsidy expenditures, Section 8 must be modified to enable HUD to reduce contract rents, not renew Loan Management Set Aside contracts, adjust rents in a simplified but rational manner instead of the current comparability system, and to recapture and reuse Section 8 authority when a contract is terminated for cause. In addition, HUD must be able to avoid the shared savings provisions of the McKinney Act for FHA properties.

Budget and Scoring Implications

The portfolio restructuring proposal (including the effects of cuts and reforms described above) is estimated to save the Federal Government money. Presentation of these savings are complicated by the fact that spending for this program includes discretionary appropriations and mandatory costs, and that the proposal is scored on a credit reform basis. Therefore, the cost is presented from two perspectives. The first examines the total cost is presented to the Government. This makes clear the financial rationale of the proposal. The second is from a Budget Enforcement Act perspective. This makes clear how the proposal complies with statutory requirements related to mandatory insurance claims costs.

From the first perspective, the proposal provides a net financial benefit to the Federal Government over a 25-year period—including a discounting of cash flows to account for the Government's cost of borrowing. This length of time is the appropriate period of analysis for covering the complete effects of the proposal. Using a shorter period would give a distorted picture of the proposal because it would capture the short-term transition costs but not fairly reflect the long-term savings resulting after that transition. In the short term, there will be relatively large outlays from paying partial claims. However, after properties are marked down, there will be long-term savings from reductions to subsidies and the avoidance of full claim payments.

Over the 5-year horizon commonly used in Federal budgeting, the proposal will increase costs to the General and Special Risk Insurance Fund because of the increased short-term transition costs. However, as displayed in the President's FY 1996 Budget, these increased costs are fully offset by the legislative proposal. The discretionary portion of the proposal (reductions to rental subsidies and other support for insured properties) was reflected in the President's Budget. The mandatory impacts (short-term increases in claim payments) were not reflected on a cash basis in the Budget, but were included when calculating the net present value impact of the proposal as a whole.

The President's Budget indicated that the proposal would be budget neutral from a "pay-as-you-go" (PAYGO) standpoint. In other words, the proposal would pay for itself under budget enforcement rules and would not require a PAYGO offset.

It is anticipated that the discretionary cuts outlined in this proposal will affect mandatory spending by increasing claim payments. In accordance with the Budget Enforcement Act, a revised baseline reflecting the effect of lower subsidies will be developed for the insurance fund after the reduced appropriations have been enacted. The budget scoring of the legislative proposal assumes that the discretionary appropriations are enacted first, and that the proposed reforms are contingent upon enactment of those appropriations.

The detailed costing of the proposal confirms what was included in the President's Budget. Recently updated estimates actually reveal that there would be net savings from this proposal. Under budget scoring procedures, however, the PAYGO impact of the proposal must conform to that in the President's Budget. As a result, the Administration would score the impact of the legislation as neutral.

The Administration is proposing that any savings generated by the reforms in this legislation be used to offset the increase in costs resulting from appropriations action affecting the FHA General and Special Risk program. The PAYGO neutral estimate shown in the President's Budget for this legislation were developed under this assumption.

C. Federal Housing Corporation Charter Act (Draft)

Explanation of the Legislation

Title XXX: Federal Housing Corporation Charter.

This Title transforms the Federal Housing Administration into a wholly owned, self-sustaining, government corporation. This Title establishes the structure of the Federal Housing Corporation (the "Corporation" or "FHC"), sets forth the Corporation's powers and authorities, establishes public purpose and safety and soundness performance requirements and a system of oversight and accountability, provides for a transition period, and provides for the repeal and termination of certain programs formerly under the jurisdiction of the Secretary of the Department of Housing and Urban Development.

Section 101: Short Title

This section will entitle this Title, the "Federal Housing Corporation Charter Act."

Section 102: Findings

This section will enumerate findings justifying the incorporation of the Federal Housing Corporation. Findings will include

- An assessment of unmet housing and housing credit needs of families, communities, and certain markets, and the relationship between housing and vibrant communities;
- A statement about the persistence of housing and lending discrimination in the Nation, and the need to ensure that housing credit provided by a government corporation is made available on a nondiscriminatory basis;
- An assessment of the health care facility financing needs of particular communities, and relationship between health care facilities and community development and empowerment;
- A statement of the historical role FHA has played in the housing finance arena, including its pioneering and market stabilizing role;
- A statement of the role FHA plays today in the system of housing and health care facility finance, and the housing and health care facility needs served by FHA today;
- An assessment of the weaknesses of FHA today and an evaluation of the impact of those weaknesses on the ability of FHA to fulfill its unique mission.
- A description of the housing finance system, how it has matured and changed, and its continuing weaknesses and strengths in meeting the needs of certain Americans and in providing capital for affordable rental housing.
- A statement of the potential critical role to be played by instrumentalities of the Federal Government in the housing finance system;
- A statement recognizing the need to benefit low- and moderate-income families, and recognizing the importance of business diversity in order to maintain self-sufficiency during an era of scarce Federal appropriations for government programs, while acknowledging the cost that would be incurred by limiting the government role to serving only low-income families; and
- A statement that, to better carry out such a role, the Federal Government entity must be structured differently: It must be flexible and entrepreneurial without reducing accountability, by building mechanisms to monitor the corporation's accomplishment of its public purposes and its ability to manage risk prudently and prevent losses

Section 103: Establishment of Corporation

(a) In general. — The Federal Housing Corporation will be established as a distinct government corporation within the Department of Housing and Urban Development (the "Department"). The Corporation will be wholly owned by the Federal Government, pursuant to the Government Corporation Control Act, and will be subject to all the provisions of that Act. The Corporation will have succession until dissolved by an Act of Congress. The Corporation will be subject to the policy direction and performance oversight of the Secretary of the Department of Housing and Urban Development (the "Secretary" of the "Department").

(b) Corporate Offices. — The Corporation will be required to maintain an office in the District of Columbia, and will be deemed a resident thereof. The Corporation may additionally establish offices in such other places as it deems necessary or appropriate in the conduct of its business.

Section 104: Purposes

The purposes of the Corporation will include the following.

- To facilitate homeownership and rental housing opportunities through the provision of credit enhancement and related activities.
- To address the unmet housing credit needs of American families and communities.
- To address the unmet health care facility credit needs of particular communities.
- To supplement and expand private sector activity by better serving underserved markets, testing new products, and filling gaps in the provision and delivery of mortgage credit.

- To deliver housing credit enhancement and provide other services in a nondiscriminatory manner, and to administer its business in a manner which affirmatively furthers fair housing.

- To promote liquidity and provide stability to the housing finance market, by continuing to provide credit enhancement on a sound basis during times of regional economic fluctuation.

- To engage in research and development of new products designed to promote housing credit to underserved markets.

- To collect and provide information relevant to the provision of housing credit to American families and communities.

- To increase the capacity of localities, States, and private and nonprofit entities in delivering housing credit to American families and communities.

Section 105: Corporate Governance

This section will create a system for corporate governance, placing the locus of powers and authorities within a Chief Executive Officer, under the direction and authority of the Secretary of the Department.

(a) Chief Executive Officer. — All powers of the Corporation will be vested in a Chief Executive Officer, appointed by the President, with the advice and consent of the Senate. The CEO will serve at the pleasure of the President. The CEO will be required to be experienced in the business of the Corporation and in the needs of underserved borrowers and communities, and will be compensated at the same level as the president of the Government National Mortgage Association, or Level IV of the Executive Schedule.

(b) Authority of the Secretary: The Corporation will be subject to the authority and direction of the Secretary, as to both policies and performance. The Secretary's oversight will ensure that the purposes of the Corporation are accomplished, the public purpose performance requirements are met, and the Corporation operates in a financially safe and sound manner. The Corporation will follow the requirements of the Government Performance and Results Act in providing management information to the Secretary.

(c) Advisory Board: The Secretary will be provided with the authority to establish an advisory board. If established, the advisory board will provide advice to the Secretary as to the policies of the Corporation and will be authorized to examine the Corporation's performance vis á vis the public purpose requirements. The purpose of establishing such a board will be to

1) obtain guidance from participants in the mortgage markets served by the Corporation;

2) assess the needs of consumers of single-family and multifamily housing, as well as the needs of communities and housing providers;

3) obtain information as to the activities of the private market, in order to better assess how to complement and partner with private and other public entities; and

4) assist the Secretary in coordinating the role of Federal housing, banking, and other credit agencies in delivering housing credit to families, communities and markets underserved by the private mortgage markets.

Members of the advisory board will include market participants, consumers, representatives of communities, and representatives of Federal banking, housing and credit providing agencies.

Section 106: Management and Personnel:

(a) Appointment of employees and officers. — The CEO will be given the authority to appoint officers and employees of the Corporation, as the CEO determines necessary to carry out the functions, powers, and duties of the Corporation.

FHA cannot hire staff quickly or effectively. It cannot procure outside skills quickly, as needed to respond to changing markets. It cannot spend a nickel on staff to save a dime in its portfolio. Finally, FHA's staff needs compete with other Department priorities, resulting frequently in management choices that inhibit FHA's ability to manage its risk prudently and that hamstring the fulfillment of FHA's mission, mandate, and effective operation.

As a government corporation responsible to the American taxpayer for prudent risk management, the FHC must have highly skilled staff that can respond to ever-changing market conditions in an entrepreneurial manner.

This section will identify the specifics of the Corporation's personnel system. The system will provide the CEO with appropriate flexibility, yet will ensure the fair, equitable, and nondiscriminatory treatment of staff. Employees of the Corporation will be Federal employees. Civil service protections and

benefits of Title 5 of the United States Code will apply except where specific exemptions are set forth. For example, the Corporation's salary schedules may mirror the comparability system retained by other Federal banking regulatory agencies. Additionally, specific exemptions will be made to ensure that the Corporation can hire, deploy, and terminate employees quickly, fairly, and effectively.

(b) FHC employees. — In general, the Corporation will employ many fewer employees than are employed by today's FHA. Downsizing will be carefully done to ensure the Corporation retains the necessary expertise and skills to perform its mission and operate in a safe and sound manner. The veterans' preference in employment will continue to apply. Additionally, as the Corporation intends to develop new lines of business and create market analysis, product development, partner oversight, and financial analysis functions not currently possessed by FHA, the Corporation will not be able to find all the necessary skills and qualifications within the existing FHA workforce.

Section 107: Procurement

The Corporation will comply with the Federal Property and Administrative Services Act, except for certain exceptions noted in this section. Currently, FHA is hampered in its ability to procure goods and services. While propriety in procurement is imperative, excessive regulation coupled with elongated bid processes and evaluations have essentially defeated FHA's ability to maximize efficiencies through procured talent and skills. In general, the Federal procurement system effectively precludes expedited operations, which are critical to a financial institution operating in complex mortgage and financial markets. The absence of speed in procurement results in losses to the Government. For example, the inordinate length of time it took (11 months) to hire a financial advisor in connection with FHA's multifamily note sales resulted in unnecessary losses due to interest rate increases. Additionally, the Corporation will need to maximize market efficiencies by availing itself of certain skills through procurement for specific functions better performed by the private sector.

The Corporation's procurement policies will be structured to ensure that the Corporation takes advantage of private sector efficiencies quickly and competently. In fact, the Corporation intends, where prudent and feasible, to engage in public/private partnerships, matching government efficiencies and economies of scale with private and other State and local public sector expertise. In this manner, the costs of providing housing credit to the underserved markets in this Nation will be minimized. With relief from certain restrictive components of the Federal Property and Administrative Services Act ("FPASA") and regulations promulgated thereunder, the Corporation can streamline and downsize the Federal Government while increasing its accountability.

The Corporation will develop a results-oriented acquisition process with quantitative and qualitative measures and standards for determining the extent to which the process effectively and efficiently supports the achievement of program objectives.

Therefore, this section will explain in detail the Corporation's procurement system. Such system will follow the broad mandate of the FPASA — including promoting competition, justifying prices, promoting fairness, and preventing waste and abuse. At the same time, the FHC's procurement system will be sufficiently and appropriately flexible to respond rapidly to changing market conditions.

Section 108: General Powers of the Corporation

Background. — The Corporation's powers will include any and all powers necessary to effectuate its purposes, and to accomplish its mandated activities. These powers will include, in connection with both housing and health care facility credit enhancement, powers related to insuring mortgages and mortgage pools, managing assets and disposing of property, and otherwise providing credit enhancement-related services, products, and information. Additionally, the Corporation will possess the general corporate powers appropriate and necessary for government corporations, as provided in the Government Corporation Control Act, to which the Corporation will be fully subject.

This section will enumerate the powers of the Corporation in connection with all lines of business and activities to be undertaken by it. In general, the new Corporation will be structured, through its powers, to be more entrepreneurial, streamlined, downsized, and accountable. The Corporation's overall business will be self-sustaining.

Specifically, the powers will include the following:

1) Corporate Name: To adopt, alter, and use a corporate seal, and to sue and be sued in its corporate name.

2) Corporate Self-Governance: To adopt, amend, and repeal by-laws, and other written administrative guidance.

3) Credit Enhancement: To enhance and make commitments to enhance credit, including commitments to lend, insure, reinsure, advance, incur liabilities, pool loans, reinsure, risk share, and securitize;

4) Business Activities — Purchase and sale of property and obligations: To purchase and otherwise acquire, including through foreclosure or eminent domain, to sell and otherwise dispose of, and to use and otherwise deal in and with, real and personal property and assets and obligations;

5) Business Activities — Agreements: To execute contracts and other agreements in its own name, with parties including any State, the District of Columbia, the territories and possessions of the United States, or with any political subdivision thereof, and Indian Tribes.

6) Business Activities — Asset Management: To take any actions necessary to manage its existing portfolio of property, assets, and obligations, including the improvement of assets, the disposition of assets, and the restructuring of debt;

7) Custody and Investment of Funds: To hold its funds in its own accounts with the Secretary of the Treasury; provided that funds not required to be held in the Financing Account (as defined in the Federal Credit Reform Act of 1990) will be invested by the Secretary of the Treasury, at the request of the Corporation's CEO, in public debt securities with maturities suitable to the needs of the Corporation bearing interest rates determined by the Secretary of the Treasury, taking into consideration current market yields on outstanding obligations of the United States of comparable maturity.

8) To determine, within the parameters of the Government Corporation Control Act and other applicable statutes, the character of and the necessity for the obligations and expenditures of the Corporation, and the manner in which such obligations will be incurred, allowed, and paid, provided that the Corporation will borrow only from the Treasury and only upon terms and conditions determined by the Secretary of the Treasury.

9) Lines of Business: To create distinct insurance funds or otherwise segregated business activities or accounts;

10) To qualify any person or party to engage in business with the Corporation, and to enforce, and to impose penalties for the breach of, obligations and other commitments made by such persons or parties,

11) To create and supply any product or service consistent with the corporate purposes, to charge reasonable fees and prices for such products and services;

12) To take actions necessary to administer its business in a manner which is nondiscriminatory and which affirmatively furthers fair housing;

13) To invest in capital, such as systems and technology, at any time after the effective date of this Act, in order to expedite the Corporation's ability to function as a going concern, and to enhance its ability to engage in the business contemplated by this Act; and

14) To have and exercise all powers necessary or appropriate to effect any of the purposes of the Act

Section 109: Public Purpose Performance Requirements; Public Purpose Overseer; Sanctions

This section will establish a series of mandatory public purpose performance requirements which must be met each year and will establish the Secretary as the overseer of the Corporation's public purpose performance. Additionally, this section will establish transition public purpose performance requirements to cover the period until the overseer develops more appropriate measures and requirements for future years.

FHA's current inefficiencies stem, in part, from prescriptive requirements that limit its abilities to fulfill its mission prudently. Performance has been measured not upon results obtained, but often, upon whether prescriptive requirements have been fulfilled. Recognizing that a results-oriented focus leads to increased accountability, Congress enacted the Government Performance Results Act of 1993 (the "GPRA"). The Corporation is designed to be a model of an accountable government activity envisioned in the GPRA.

To provide the utmost accountability to the taxpayer, the Corporation will, for the first time in FHA's history, be measured for effectiveness based upon its results, in two distinct areas: 1) fulfillment of public purpose requirements will ensure that the Corporation effectively uses its special government status to produce public benefits, while minimizing competition with the private sector; and 2) achieving safety and soundness requirements will ensure that the Corporation's mission is accomplished without exposing taxpayers to undue risk of loss.

In 1992, Congress enacted the Federal Housing Enterprises Financial Safety and Soundness Act. This Act placed public purpose and safety and soundness requirements upon two housing government-sponsored enterprises ("GSEs"): the Federal National Mortgage Association, and the Federal Home Loan Mortgage Corporation. The GSE public purpose goals were established, in part, in response to Congress's recognition

that the GSEs were assigned in their respective charters an affirmative obligation to facilitate the financing of affordable housing for low- and moderate income families while maintaining a strong financial condition and a reasonable economic return. Congress recognized that public purpose business could create a good return for private investors.

The requirements established under this section are similar to those established in 1992 in connection with the GSEs. However, they also differ significantly, in both the substantive focus of the requirement (what is measured) and the level of performance demanded (the proportion of business devoted to public purposes). The difference is partially attributed to the fact that the GSE business will be different from that of the Corporation. The difference also reflects the different ownership structure of the Corporation vis á vis the GSEs. Namely, the GSEs are privately owned with private shareholders, while the Corporation will be a wholly owned government corporation, not accountable for producing economic return to private shareholders. Therefore, to the extent that both the Corporation and the GSEs are required to reach markets underserved by the conventional market through similar performance requirements, the level of public purpose performance required of the FHA will in most instances be higher than that required of the privately owned GSEs.

(a) Public Purpose Requirements. This subsection will establish a number of performance requirements ensuring that the Corporation provides housing credit or credit enhancement which benefits families, communities, and markets underserved by the private mortgage markets. The level of performance that will be required under each requirement will ordinarily be no less than FHA's level of performance in connection with each measure during 1994.

1) Underserved homebuyers: This requirement will measure performance in connection with credit or services provided to certain families who otherwise find it difficult to attain homeownership, such as first-time homebuyers, minorities, immigrants, young households lacking savings, and low-income households. The entire market, including FHA, must do better to enable all families to achieve the dream of homeownership.

2) Underserved areas: This performance requirement will measure the Corporation's provision of credit or services to certain underserved geographic regions. Analyses of mortgage flows demonstrate that mortgage originations and mortgage declines are highly correlated with the median income or racial composition of a neighborhood. Geographic areas typically underserved by the private mortgage markets could include portions of central cities, suburban areas, and rural areas.

3) Underserved rental markets: This requirement will measure the Corporation's performance in connection with providing credit or services that benefit renters and rental markets. Currently, the stock of privately owned affordable rental housing is dwindling, through age, deterioration, lack of capital, and inadequate replacement. Multifamily housing finance is complex, lacks standardization, and each financing package must be structured to meet the needs of individual neighborhoods. This requirement, therefore, could measure products or services benefitting large families and very low income families, or small properties or properties located in underserved neighborhoods.

4) Low- and moderate-income families: This requirement will measure the Corporation's provision of credit or services, in both the single- and multifamily arenas, to low- and moderate-income families and individuals.

(b) Transition Period Public Purpose Requirements.— Because more analysis will be needed in order to determine the appropriate focus and level of each requirement, the transition period public purpose requirements will reflect proxies for each requirement set forth in (b). The following requirements will be established as transition period public purpose requirements.

1) Underserved homebuyers: Mortgage credit afforded to first-time homebuyers;

2) Underserved areas: Credit or services benefitting underserved areas as defined by regulation in connection with the underserved areas affordable housing goal applicable to the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation;

3) Underserved renters or rental markets: Mortgage credit or benefits afforded to very low income families; and

4) Low- and moderate-income families: Mortgage credit or benefits afforded to low- and moderate-income families.

The level of performance required for each transition period requirement will be no less than the level of performance achieved by FHA in 1994.

(c) Authority of the Secretary. — In addition to providing general policy oversight and direction to the Corporation, the Secretary will be specifically charged with overseeing the Corporation's public purpose performance. As overseer, the Secretary will be authorized to make such rules and guidelines as will be necessary and proper to ensure that this section and the purposes of the Corporation are accomplished. In establishing the public purpose requirements, and modifying them from time to time, the Secretary will consider factors including: national housing needs; economic, housing, and demographic conditions; the performance of the Corporation in prior years; the size of the FHA-eligible conventional market serving families and communities identified as underserved; and the need to maintain the financial safety and soundness of the Corporation.

(d) Enforcement of Public Purpose Requirements. — This subsection will establish the procedures to be used by the Secretary upon the Secretary's determination that the Corporation failed to make a good faith effort to comply with the requirements of this section. Specifically, the Secretary will be authorized to take appropriate actions if

1) the Corporation fails to make a good faith effort to comply with the requirements of this section;

2) the Corporation fails to make a good faith effort to submit or complete reports required by the Secretary in conjunction with determining compliance with this section, and

3) the Corporation engages in or is about to engage in conduct that violates the charter of the Corporation.

Section 110: Financial Safety and Soundness; Transition Period Requirements; Safety and Soundness Regulator; Sanctions

Background. — Currently, FHA prepares an audited financial statement prepared in accordance with generally accepted accounting principles (GAAP). In FY 1993, FHA received its first clean opinion on its financial statements since the Chief Financial Officer's Act was enacted. However, Congress primarily assesses FHA's financial performance by reference to two static measures: the capital ratio of the Mutual Mortgage Insurance (MMI) Fund and the multifamily loss reserve.

In 1990, Congress required that the MMI Fund, in which most of FHA's single-family business is conducted, be subject to an independent actuarial study each year and achieve a capital ratio of 1.25 percent by the year 1992 and 2.0 percent by the year 2000. In FY 1993, a Price Waterhouse actuarial study found that the MMI Fund had a capital ratio of 1.44 percent and would achieve a ratio of 3.40 percent by the year 2000.

FHA also prepares an annual evaluation of the health of its multifamily insurance portfolio and sets aside for financial statement purposes a reserve against anticipated losses. In FY 92, the multifamily loss reserve was $11.9 billion against approximately $43.5 billion in insurance-in-force. In FY 93, the loss reserve dropped to $10.3 billion against a portfolio of $43.9 billion in insurance-in-force. All actual losses in the current multifamily program are supported by a permanent indefinite appropriation.

The new Corporation's overall business will be self-sustaining. However, given the past performance of some of FHA's lines of business, the changes proposed in its product line, the commitment to serving markets under-served by the private mortgage markets, and the magnitude of its potential operations, public acceptance of a new corporation with broad and flexible insurance authorities requires a strong system to ensure that safety and soundness will be adequately monitored and reported independently of the Corporation directly to the Secretary, the President, and Congress.

Safety and soundness, as measured by a safety and soundness regulator, will include the measurement of actuarial soundness as well as additional indicators of financial integrity. The measures will be applied to single-family, multifamily, and health care facility businesses, and will allow those lines of business that generate more revenue to support less profitable lines of business, provided that the overall capital requirements are met. The safety and soundness regulator will therefore measure the actual risks of the Corporation's business, the safety of its operations and management, and the required level of capital sufficient to support the entire corporation's business.

This section establishes the safety and soundness performance measurements as well as the safety and soundness regulator who will monitor that performance.

(a) Financial Accountability and Safety and Soundness Goals. — The safety and soundness regulator will design and operate a system for establishing financial safety and soundness performance requirements designed to ensure that the Corporation is capable of covering anticipated expenses and losses and protecting the taxpayer against unanticipated losses. Specifically, in addition to maintaining reserves against anticipated

losses for outstanding books of business, the Corporation will be required to maintain a certain level of additional capital, as determined under a risk-based capital adequacy model developed by the safety and soundness regulator, described in (c). The model will evaluate the risk of individual business lines; however, the capital adequacy of the Corporation will be determined based on the activities of the Corporation as a whole, rather than on a business-by-business basis. The goal of the model is to ensure that the risks undertaken by the Corporation are prudent and appropriate to the Government's fulfillment of its role in the housing credit market.

(b) Transition Period Financial Accountability and Safety and Soundness Requirements — During the transition period, the safety and soundness regulator will develop an interim capital adequacy model, after consultation with the Secretary, to be used in connection with the business entered into by the Corporation under new credit enhancement authorities provided in this Title. These standards will be used for determining the Corporation's compliance with the requirements of this section until such time as the risk-based capital adequacy model is completed. No new business under the new authorities provided in this Title may be undertaken by the Corporation until these standards are in place.

(c) Financial Safety and Soundness Regulator. —

1) The Director of the Office of Federal Housing Enterprise Oversight ("OFHEO") will be the financial safety and soundness regulator (the "safety and soundness regulator") of the Corporation.

2) The powers and duties of the safety and soundness regulator will be exclusive of the Secretary, and will include

(A) Development and application of a risk-based capital adequacy model to assess the performance of the Corporation's entire outstanding portfolio and reserves, through simulations which would assume both the Administration's economic forecast and more severe economic conditions;

(B) Development and application of an interim capital adequacy model;

(C) Performance of regular examinations of the Corporation's financial condition and risk management structure and techniques;

(D) Analysis of historical data on the performance of mortgages insured by the Corporation;

(E) Authority to use enforcement actions set forth in Subsection (d);

(F) Authority to require the Corporation to submit reports determined by the regulator to be necessary to carry out the purposes of this section; and

(G) Use of models under (A) and (B) to comply with the duties required of the safety and soundness regulator set forth in Section 111.

(d) Enforcement Provisions. — This subsection will establish the procedures to be used by the safety and soundness regulator, upon the regulator's determination that the Corporation failed to achieve the capital requirements established by the safety and soundness regulator. Specifically, the regulator will be authorized to take enforcement actions upon a determination that

1) the Corporation failed to comply with the requirements of this section or with written agreements executed between the Corporation and the safety and soundness regulator, or to submit or complete reports required by the safety and soundness regulator in conjunction with determining compliance with this section;

2) the Corporation engaged in or is about to engage in conduct that ultimately threatens the adequacy of the Corporation's capital, and

3) the Corporation failed to take certain affirmative actions, required by the safety and soundness regulator in response to specific conditions to be enumerated in this paragraph, to remedy undercapitalization.

(e) Funding. — This subsection would establish the mechanism that will fund the safety and soundness regulator's operations in connection with the Corporation.

(f) Reports. — This subsection will set forth the types of reports required to be submitted by the safety and soundness regulator to the CEO, the Secretary, the President and the Congress, and the timetables required in connection with submitting reports sufficient for purposes Section 111(b).

Section 111: Budget Process; Federal Credit Reform

This section will set forth the procedures and timetables pursuant to which the Corporation's practices will satisfy the Federal Credit Reform Act.

Background. — Title V of the Congressional Budget Act, the Federal Credit Reform Act of 1990, requires the advance budgeting of all estimated costs arising from direct loan obligations and loan guarantee commitments made after 1991. Compliance with this Act ensures that Congress is accountable in any one year for the entire cost that will be incurred in Federal credit programs over the life of the credit or credit guarantee. This Act was intended to ensure that future losses would be supported through the revenues of the credit programs or through contemporaneous appropriations. Government business-type programs that generate sufficient revenues to cover obligations do not rely upon appropriations; compliance with the Federal Credit Reform Act's goals in such cases conforms the program's business accounting with the budget process of the Federal Government.

The new Corporation is intended to be self-sufficient. The safety and soundness regulator's primary role will be to determine whether or not, at any given time, there is sufficient capital reserved for the outstanding books of business. However, it is imperative that the methods used for assessing the adequacy of the capital reserves are not inconsistent with the methods used by the Director of the Office of Management and Budget to estimate credit subsidy for purposes of reflecting the Corporation's activity in the Federal Budget. Operating a business under two conflicting regimes could result in decisionmaking that would inhibit the Corporation's ability to accomplish its public purpose mission.

As described in Section 110, the safety and soundness regulator will use the risk-based capital adequacy model or interim model, as applicable, to determine the expected performance — including expected income, claims, losses, and net earnings — for the outstanding portfolio under various economic assumptions. This same approach also will be used by the safety and soundness regulator to evaluate in advance the annual business plan of the new corporation using the President's economic forecast. The regulator will determine whether business under the plan would cause the Corporation to fail to achieve the capital required under the risk-based capital adequacy model or interim model.

To make this determination, the risk-based capital adequacy model or interim model, as applicable, applied by the safety and soundness regulator will generate estimates of performance — based upon the Corporation's anticipated volume, income, claims, losses, net earnings, and the Administration's economic forecast — for new business to be conducted under that year's business plan as well as for the outstanding portfolio. These estimates of performance will serve as the basis for the credit subsidy cost estimates that will be used to reflect the Corporation's activity in the President's budget. Using this process, the safety and soundness regulator will produce the credit subsidy cost estimates and will provide them to the Corporation. The Corporation, which has the ultimate responsibility for providing the subsidy estimates to the Office of Management and Budget, will submit those estimates to the Director of the Office of Management and Budget for use in the President's Budget.

(a) Annual Budget Reporting Requirements. — The Corporation will establish procedures to submit the annual budget and business plan to the safety and soundness regulator in a time period sufficient for producing the credit subsidy cost estimates required for the President's budget, in accordance with the Government Corporation Control Act. The Corporation's procedures will provide for the Secretary's submission of an annual budget and credit subsidy cost estimates to the Office of Management and Budget to be reflected in the President's Budget.

(b) Annual Credit Reform Cost Subsidy Estimates. — The Director of the Office of Management and Budget will utilize, for purposes of the President's annual budget, an annual credit subsidy cost estimate for the Corporation based upon the credit subsidy cost estimates produced by the safety and soundness regulator and submitted to the Director by the Secretary.

All credit subsidy cost estimates will be "unified." Although the safety and soundness regulator will assess the performance of, and apply the risk-based capital adequacy model or interim model to individual lines of business, the credit subsidy cost estimates will be reported in connection with the Corporation's business, as a whole. Such unified estimates will permit the Corporation to engage in varied business lines so long as its overall performance satisfies the strict risk-based capital adequacy standards defined by the safety and soundness regulator. This approach will enable the Corporation to serve underserved and untested markets, while operating on a self-sustaining basis, covering future losses, and minimizing risks to the government and the taxpayer.

Section 112: Authorization of Appropriations

(a) Annual appropriations of retained earnings. — The Corporation will be self-sustaining. However, in order to be self-sustaining, it must retain the ability to invest any of its earned revenue back into its reserves or, among other uses, to support its operations or more targeted service to markets and borrowers underserved by the private market. In this section, the Corporation will be authorized to receive an annual appropriation of an indefinite amount which will be equal to the negative

subsidy generated by the Corporation in any year. This appropriation is not an appropriation of Treasury general funds; rather, it is a return to the Corporation of income to the Government that the Corporation has generated. This appropriation will boost the Corporation's safety and soundness by allowing it to build reserves to cover losses resulting from any current or future business or to invest in technology and infrastructure. Because of the nature of the housing credit business, it will be critical for the Corporation to place its yearly earnings in reserves dedicated for these purposes. Any displacement of such funds would jeopardize the Corporation's ability to function as a housing credit business, to honor its commitments, and to operate as a going concern beyond each fiscal year.

(b) Appropriation to cover certain activities that conflict with Corporation's ability to be self-sustaining. — The Corporation will be authorized to receive appropriations necessary to cover the costs of engaging in certain activities mandated or authorized by statute enacted after the effective date of this Act, if such activity is not expected to be self-sustaining, and if such activity has not been anticipated by the Corporation. The Corporation will be prohibited from engaging in any such mandated activity unless it receives sufficient appropriations.

Section 113: Capitalization and Guaranty

This section will establish a mechanism for the initial capitalization of the Corporation and will designate the sources of capital to serve as initial capital. The Corporation will be authorized to receive an appropriation for the purpose of initial capitalization.

This section will also state that obligations of the Corporation will be backed by the same level relationship to the U.S. Treasury as are obligations of today's Federal Housing Administration.

Section 114: Evaluation of Potential Partners and Other Participants

To maximize its efficiency and the benefits accruing to families and communities underserved by the conventional mortgage markets, the Corporation, where prudent and feasible, will rely upon private and other public partners and business participants in different capacities. One type of partnership will be risk-sharing arrangements, under which the FHC will share the risk of default with another well-capitalized institution. FHA currently retains demonstration multifamily risk-sharing authority which allows it to enter into agreements with State and local housing finance agencies, government-sponsored enterprises, and others.

The risk-sharing partnerships in which the new Corporation will engage will cover both the single-family and multifamily arenas, with current partners and new partners. Partners would include private mortgage insurers, State and local housing finance agencies, government-sponsored enterprises, including Fannie Mae, Freddie Mac, and the federal home loan banks, and other private and public entities determined by the CEO to meet the requirements established in this section. Such risk-sharing arrangements have permitted FHA under certain circumstances to delegate processing, underwriting, and asset management and disposition functions to partners, resulting in financial and administrative savings to the Government, and further insulating taxpayers from losses.

The Corporation will establish guidelines to be used in evaluating the capacity of potential partners and other participants. Guidelines in connection with potential risk-sharing partners will be consistent with the following goals:

1) To ensure that partners are fully capable of fulfilling their obligations to the Corporation.

2) To ensure that partners are sufficiently capitalized and retain sufficient creditworthiness to cover future obligations;

3) To ensure that the general business of partners does not conflict with the mission of the Corporation.

4) To maximize efficiency and effectiveness in product delivery and operations; and

5) To minimize losses to the Federal Government.

Section 115: Corporate Guidelines and Practices

The Corporation will develop business rules, guidelines, and practices governing its business and operations. To prudently address business concerns within the context of a rapidly changing housing finance arena, the Corporation will retain the ability to continually revise its rules, guidelines, and practices. To accommodate this flexibility, the Corporation will be exempt from most of the rulemaking requirements of the Administrative Procedures Act. Additionally, in connection with their respective roles as overseers or regulators of the Corporation's performance requirements, the Secretary and the OFHEO Director will be exempt from most of the rulemaking requirements of the Administrative Procedures Act. Finally, any rule or regulation issued by the Secretary with respect to the Department will not apply to the Corporation unless the Secretary specifically finds that application of such rule or regulation to the

Corporation is consistent with the Corporation's achievement of its mission

Section 116: Oversight and Reporting Requirements

Most of the oversight specified in this section is derived from the Government Corporation Control Act. These requirements are in addition to internal procedures the Corporation will undertake to minimize risk and ensure the integrity of operations. For example, the Corporation will establish an internal audit office.

(a) Audited Financial Statements. — The Corporation will be required to submit to the Secretary, the safety and soundness regulator, the President, and Congress annual audited financial statements, prepared in accordance with generally accepted accounting principles, performed by a qualified independent third party and conducted in accordance with generally accepted auditing standards.

(b) GAO Audit. — The Corporation will be required to submit any financial, operations, or other information, as needed, to the Comptroller General of the United States, pursuant to the existing Federal audit powers of the Comptroller General.

(c) Annual Budget. — The Secretary will be required to submit an annual business-type budget of the Corporation to the Director of the Office of Management and Budget in a way, and before a date, the President prescribes for the budget program, pursuant to the Government Corporation Control Act

(d) Annual Business Plan. — The Corporation will be required to submit an annual business plan to the Secretary for the Secretary's approval. The business plan will specify the product and operational strategy of the Corporation, including plans to address compliance with the performance requirements. The approved business plan will be submitted by the Secretary to the safety and soundness regulator.

(e) Quarterly Reports. — This subsection will require the CEO to submit quarterly reports as to financial information and business volume to the safety and soundness regulator and the Director of the Office of Management and Budget, and will explain that submission of such reports will satisfy the apportionment requirements of the Antideficiency Act.

(f) Annual Report on Performance. — The Secretary and the safety and soundness regulator will each submit an annual report to Congress on the Corporation's performance as measured by the performance requirements

(g) Inspector General. — The Inspector General of the Department of Housing and Urban Development will perform the functions of Inspector General for purposes of this Title.

Section 117: Limitation on Business Activity

The Corporation will be subject to two overall business limitations:

1) a maximum mortgage amount, which will be set at and adjusted pursuant to the statutorily imposed limit; and

2) an aggregate 5-year new business volume limitation, which will commence upon the Corporation's execution of new business under new authorities pursuant to Section 120(b)(2).

Section 118: Penalties

This section will specify the array of penalties available to the Corporation for the purpose of sanctioning partners and other participants who fail to comply with program requirements or with the terms of their obligations to the Corporation.

Section 119: Applicability of Other Federal Statutes

This section will provide that, unless otherwise specified in this Act, the Corporation will comply with all applicable statutes. Exemptions will be listed in this section based upon a finding that compliance with such statute is incompatible with the Corporation's ability to accomplish its purposes in a safe and sound manner.

Section 120: — Transition Period

(a) In general. The Corporation will operate subject to transition period authorities set forth in this section. The transition period will commence upon the date of incorporation, which will be the effective date of this Act. During the transition period, the Corporation will invest in new capital systems and infrastructure, develop a detailed business plan and rules and guidelines governing the Corporation's new business operations, reduce the overall number of employees to meet the President's goals while ensuring adequate skills to safely and prudently conduct the new business of the Corporation, and phase out certain operations under pre-existing insurance authorities. During this transition period, the Corporation will continue to issue mortgage insurance and enter into risk-sharing arrangements under available authorities, and begin to undertake new business under the authorities set forth in this Title.

(b) Business Activities During the Transition Period.

1) Continuation of business under authorities existing prior to the date of incorporation. Upon the Secretary's delegation to the CEO, pursuant to Section 121, of pre-existing authorities and powers, the Corporation may engage in new business authorized under such pre-existing authorities. To the extent that any new loan originations are made by the Corporation in connection with such authorities, the Corporation will be required to comply with existing statutory capital requirements in connection with pre-existing insurance funds as of the date of enactment of this Title.

2) Commencement of new business under new authorities. This paragraph will create "triggers" pursuant to which the Corporation's ability to engage in new business under new authorities will be determined. Once the triggers are met, the Corporation could enter into new business under both new and old authorities. The Corporation will be authorized to enter into new business under authorities contained in this Act only upon the following:

(A) A business plan must be approved by the Secretary.

(B) The safety and soundness regulator must establish a risk-based capital adequacy model or appropriate interim model.

(C) The Director of the Office of Management and Budget must certify the risk-based capital adequacy model, or appropriate interim model, if applicable, to be consistent with the Federal Credit Reform Act of 1990, prior to initial usage by the safety and soundness regulator.

(D) The Secretary, in conjunction with the CEO, determines that the Corporation's staff, systems, and administrative infrastructure are sufficient to carry out its operations.

Section 121: Transfer Authorities, Continuation of Contracts, Orders, Proceedings, and Regulations

(a) Delegation from the Secretary. — The Secretary will be authorized to delegate to the CEO any of the functions, powers, or duties of the Secretary (with respect to the Federal Housing Administration), including the ability to be compensated, to receive appropriations, and to deal with any assets or liabilities of any fund authorized under the National Housing Act. The purpose of this delegation will be to permit the Corporation to operate selected existing FHA programs during the transition period until the businesses of the new Corporation can be fully established.

(b) Continuation of Contracts. — This subsection will permit the Corporation to continue all contracts, agreements, and other privileges, which pertain to the business of the Corporation after the date of enactment and which were formerly executed with the Department as if the Corporation had executed such contracts, agreements, and other privileges.

Section 122: Termination of Single-Family National Housing Act Programs

The Secretary, in conjunction with the CEO, will be required to make a determination as to the ability of the Corporation to operate fully as a going concern. No business operating under the existing insurance funds will be permitted to cease until this determination has been made. Upon the making of such determination, the Secretary will be authorized to terminate new business executed under the Mutual Mortgage Insurance Fund.

Section 123: Termination of Multifamily National Housing Act Programs

The Secretary, in conjunction with the CEO, will be required to make a determination as to the ability of the Corporation to operate fully as a going concern. No business operating under the existing multifamily insurance funds will be permitted to cease until this determination has been made. Upon the making of this determination, the Secretary will be authorized to terminate new business executed under the General Insurance and Special Risk Insurance Funds.

Section 124: Amendments to the Charter of the Government National Mortgage Association

The Government National Mortgage Association ("Ginnie Mae") will continue to guarantee securities backed by pools of mortgages insured under the National Housing Act, including those to be insured by the Federal Housing Corporation.

The Ginnie Mae charter will be amended to permit the excess of revenues over both expenses and provisions for losses to be transferred to the MMI fund to ensure that the MMI fund meets statutorily required capital standards.

Ginnie Mae's charter will also be amended so that the provisions of Federal rulemaking, procurement, and personnel statutes applicable to Ginnie Mae mirror those applicable to the new Federal Housing Corporation

Currently, the Treasury Department, Ginnie Mae, the Federal Housing Administration, and the Office of Management and Budget are studying the impact of having Ginnie Mae participate in risk-sharing arrangements between the Federal Housing Corporation and various private and other public entities. Any Federal Housing Corporation risk-sharing activity in which Ginnie Mae participates would be aimed at FHA's traditional market and support achievement of the Corporation's public purposes of serving underserved families, communities and markets. The result of this study will determine whether any additional changes to Ginnie Mae's charter are necessary

Section 125: Evaluation by the Secretary

Upon the first day of the third calendar year after the Corporation has commenced new business under authorities contained in this Title, the Secretary will submit an evaluation of the Corporation's activities to the President and Congress. The evaluation will include the following

1) Whether the Corporation's charter provides the necessary powers and authorities for the Corporation to accomplish its public purpose mission in a safe and sound manner,

2) Whether the business activity limitations set forth in Section 117 are consistent with the Corporation's ability to fulfill its public purpose mission in a safe and sound manner. This assessment will determine the impact of these limitations upon the Corporation's current and anticipated future business activity; and

3) Whether the performance requirements established under the charter appropriately measure (1) safety and soundness; and (2) fulfillment of the Corporation's public purposes.

Based upon the results of the evaluation, the Secretary will make recommendations for any changes determined to be necessary to the Corporation's charter.

Chapter 4: Managing HUD for Quality Performance and Results

A. Guiding Principles

Implementing HUD's reinvention plan requires continued focus to correct the significant management deficiencies, systems impediments, and problems in quality control of programs that for more than a decade have hampered the ability of the Department to fulfill its mission. HUD initiated its reinvention to address significant organizational and program deficiencies. The reinvention incorporates performance measurement and financial accountability to improve program management and delivery systems. These principles of reinvention drive HUD's management efforts.

HUD's approach to assessment and problem resolution, creating an organization that can deliver on its mission, has been guided by three key management strategies:

- Build an Effective Management Structure
- Improve Business Processes
- Improve Workforce Skills and Human Resource Management

HUD's Reinvention Blueprint continues the transformation of the Department into an entrepreneurial, customer-driven, results-oriented organization. However, it is important to emphasize that HUD's Reinvention Blueprint is built primarily on existing programs and activities which are being managed by experienced staff currently on board; many of the activities HUD is proposing are already underway at some level, and technology and training to support the reinvented HUD have been under development for some time.

Consolidation and devolution will change the way HUD interacts with families and communities, and, consequently, decrease the number of staff and dramatically change the types of skills required to maintain productive relationships. The transition to the new HUD will include consolidation of 60 programs to 7 in 1996, and existing program offices (e.g., Community Planning and Development, Public Housing) continuing to be responsible for those consolidated programs. By 1998, further consolidation will result in just 3 programs to be administered through field offices organized along functional lines (e.g., customer support, operations), providing more efficient and seamless customer service.

With fewer programs to administer, it will be possible to consolidate HUD's operational and administrative support functions for economies of scale and more efficient program administration and organizational management. HUD has several initiatives underway to prepare the Department to meet the needs and requirements of the future, particularly in the areas of technology development and workforce training.

Rationale to Support Reduced Field Structure

The consolidation and restructuring of 60 major programs into 7 and then 3 flexible, performance-based funds will result in fewer administrative and processing requirements for both localities and the Department. As a result, the Department will be able to improve its customer service through less onerous requirements, greater local responsibility and flexibility, and less direct HUD involvement. This will be achieved efficiently and effectively with a substantially reduced number of employees and with fewer field offices.

The Department will provide quality customer service through three streamlined programs and significant use of improved technology. As a result of these program and technological changes, our analysis shows the need for approximately 60 field offices. This will allow the Department to meet its responsibilities by having a HUD presence in each State, with a second office in several larger States. The size of the field offices which remain will vary according to the needs of the jurisdiction served.

The establishment of FHA service centers will greatly enhance the timeliness and quality of service to housing clients. In addition, Community Planning and Development and Public Housing program consolidation and simplification will lead to improved service to localities and tenants. Through the use of consolidated planning, the Department will ensure a more efficient use of its resources. Rather than being prescriptive, this process will enable the Department to adjust its programs to local needs.

The transition to the revised field structure will be phased in over a 2 to 4 year period.

Consolidation of Functions

Major consolidations will become feasible in earnest with the enactment of the new programs. The reduction

decisions were not linked to key management processes, such as strategic planning and budgeting, and HUD's management plans were not performance driven. Over the past decade, HUD had not kept pace with changing management structures and new technologies.

The Department has made substantial progress in developing a **Strategic Performance System (SPS)** which will support HUD's changing role and mission. Comprehensive management planning is key to the SPS and requires the development of management plans, the incorporation of management controls in these plans, the oversight of the Management Committee, and performance reporting and accountability.

Strategic performance planning, which links key policy-making, budget, and management processes, is advancing the many initiatives that have already been undertaken as part of a coherent unified approach to achieving the Department's mission. The strategic performance planning process will enable HUD to better manage its resources and processes, and to achieve a greater level of service to its constituencies.

II. Tools to Improve Business Processes

In 1992, many of HUD's programs were characterized as "process-driven" rather than "performance-driven." HUD's business practices had remained virtually unchanged since the 1980's, despite dramatic changes in the marketplace. HUD's programs, business processes and operations are being reengineered to be more responsive, reduce costs, and improve the quality of HUD's services.

The Department has implemented numerous business process improvements, including:

Analytical Process Tools

- A Departmentwide Business Process Redesign program has been implemented. HUD has developed analytical process tools to improve the processes, techniques and technology used in doing business (e.g., Business Redesign Process (BPR), Best Practices, Value Management, and Benchmarking). Several management studies for improved resource planning and performance have been undertaken, including:

  — Fair Housing & Equal Opportunity: BPR
  These efforts were recently awarded with a "Hammer Award" from the National Performance Review and President Clinton for innovative business redesign initiatives.

  — Government National Mortgage Association (GNMA): BPR
  This undertaking has resulted in GNMA initiating several opportunities suggested by the BPR, including reorganization and redefined contractor/staff responsibilities to improve the delivery system, and reconsideration of transfer fees to increase business activity.

Technology Tools

- The Technology Investment Board (TIB) was created to improve technical decisionmaking and allocation of information systems resources departmentwide. The TIB drove the FY 1996 Budget process and is the clearance point for information systems decisions. This structure supports a comprehensive and flexible approach to information systems development and expenditures to meet future needs.

- The use of Electronic Data Interchange (EDI) eliminates paper flow between HUD and its customers, supports more accurate transactions, and requires less staff resources. EDI is currently being utilized in FHA single-family programs, and its use will grow significantly in the coming months.

- The Strategic Information System (SIS) allows HUD and its grant recipients to use the same baseline data in the planning process and reduces duplicative reporting by the grantees. The SIS will be the framework for all of HUD's new grant programs by the end of 1996. It allows the grant recipient to submit a single, strategic, consolidated plan to HUD in an automated format. This system is currently in use in HUD's Office of Community Planning and Development to manage the HOME and CDBG Programs.

- Increased use of technology in administrative processes will consolidate human resource and accounting functions, and automate aspects of the contracting process. These improvements will support more efficient processing with fewer staff resources.

III. Tools To Improve Workforce Skills and Human Resource Management

In 1993, HUD did not have a comprehensive training strategy to address critical skill shortages at HUD. The continued decline in staffing levels without offsetting management improvements and staffing realignments heightened concerns about staff shortages in key programs. Management at HUD has been stymied over the last decade by a lack of useful information and the

of 60 programs to 3 will permit consolidations of such activities as grant application review, grant approval, program monitoring and administration of existing grants. These can be brought together within HUD's current organizational structure and provide the means for substantial reductions in staff by FY 2000

The need will be reduced for specialized expertise in individual programs as the number of programs themselves are reduced. Fewer staff now engaged in the preparation of regulations and notices of fund availability (NOFA) will be needed. Within headquarters and field offices, smaller staffs will be able to work with grant recipients on a broader basis than that required now with the many individual programs now in operation. The potential consolidation of program skills will also substantially lessen the paper volume demanded from grant recipients and call for less detailed reviews of programs operated by State and local governments. The emphasis on furnishing a broad-spectrum view of program assistance to grantees will mean fewer staff, but persons will have more generalized skills. This consolidation of skills can be initiated within the current organizational framework and will be more flexible and adaptable for the future mission of HUD field offices

Support Functions The restructuring of HUD's programs will also be consistent with other work now underway to consolidate administrative support functions. Administrative support functions will be under the authority of the Office of Management, which will include a Chief Information Officer. The CIO will be responsible for systems integration across the Department. Significant advances in technology, notably in communications and automation, make possible the combining of administrative support functions in fewer offices. When HUD's organization included ten regions, each of the regions included an office responsible for a full array of administrative functions: personnel, ADP, accounting (under the Chief Financial Officer), budgeting, administrative services, etc. Many of these were duplicated at field offices when slower communications and geographic distance required on-site support.

The elimination of the regional tier has removed the need for ten separate administrative centers and many more at field levels. Relying on modern technology, the Department now is preparing to establish three administrative service centers in New York, Atlanta and Denver. These will provide the full range of services. Meanwhile, administrative-staff on site in field offices will be reduced as the offices are consolidated into larger ones and support can be provided directly from the service centers

Accounting functions, under the Chief Financial Officer, are crucial to HUD because of the financial nature of the Department's programs. Concomitant with the reduction in active programs will be continued change and improvement in accounting systems. Modern technology will permit the reduction of accounting offices from the present ten in the field, in addition to headquarters. Using the kind of ADP support typical in large corporations, a reduction in the number of accounting centers to three or less is now feasible

Reductions in staffing are a logical consequence of these consolidations. As they are phased in, with an eventual reduction to about 7,500 in the salaries and expenses account, a leaner, more efficient HUD should be the result. The offering of 1,245 buyouts is a first step in the reduction of staff and the movement to consolidations

Several other options are available to support downsizing efforts. A hiring freeze was initiated on October 27, 1994. Any exceptions to the freeze must be approved by the Deputy Secretary. Normal attrition and early retirement opportunities, which will be available until September 30, 1995, will also contribute to a downsized HUD.

The transition to a smaller organization will be managed through redeployment and retraining of HUD staff. Several tools have been developed to support human resource management and workforce training. These tools are discussed in greater detail below

B. Tools For The New HUD

In the past 24 months, HUD has undertaken a decisive and organized process of evaluating and correcting systemic problems that have hampered the ability of the Department to plan for and respond to customer needs. The objective is to ensure that HUD's programs and services developed through reinvention will reach its customers and ultimate beneficiaries in a responsive and timely manner.

The following highlights key actions and specific projects undertaken within the strategic framework which shapes our efforts.

1. Tools to Build an Effective Management Structure

In 1992, HUD lacked the institutional ability to respond to the changing needs of the communities it serves. HUD's management and information systems were dysfunctional. The Department was unable to develop accurate budget estimates for key programs. Policy

absence of analytical tools necessary to accurately allocate HUD's resources in accordance with its business requirements.

The following actions have been taken to realign and retrain HUD's workforce to adapt to changing institutional demands and to develop more valuable management information systems and resource management tools.

HUD Training Academy

- The HUD Training Academy was established in January 1994. The Academy leads a coordinated, comprehensive approach to employees training and development, across a wide range of subjects and venues. It was a key factor in the substantial increase from FY 1993 to FY 1994 in the number of hours of training provided to HUD employees and intermediaries (246,000 hours to 648,000 hours).

  The Training Academy serves a critical role in preparing employees to meet the workforce needs of the new HUD. HUD's relationship with its customers and service delivery system are both changing dramatically, the Academy is the linchpin for the training and skills development that staff will need. Several of the Academy initiatives to support the training and human resource development activities required by the new HUD are described below.

Distance Learning

- The HUD Training Academy began implementation of distance learning and information sharing broadcasts through the HUD Television Network to deliver training more quickly and cost effectively, with higher quality and greater consistency. Distance learning technology has lowered travel expenses for FY 1994 by 5 percent compared to FY 1993, with an increase of approximately 110 percent in program technical training
  opportunities. Distance learning sessions are conducted several times each week on both technical and information programming topics. Distance learning will be used more extensively as HUD retrains employees about new programs and responsibilities.

University Partnerships

- The HUD Training Academy established partnerships during FY 1994 with the University of Maryland, the University of the District of Columbia, and the University of Arizona, each providing training for HUD employees in specific geographic and program areas. Several other university partnerships are under consideration.

Individual Development Plans

- A system of Individual Development Plans (IDPs) was created for all employees. These IDPs serve as the basis for analysis of current skill levels and staff training needs, and will provide information for training curriculum development decisions. The system also includes identifying and training IDP Coordinators and Career Coaches and establishing the Career Counseling Center and Mentoring Program.

Resource Management and Planning

- Resource management and planning tools have been developed to analyze resource requirements and utilization patterns in order to develop and implement organizational workload management and staffing allocation strategies. Staff Management and Assignment Review Tool (SMART) and Workload Assessment System (WAS) are computerized models which utilize artificial intelligence to assist managers in assessing staff to address the most critical program activities and make employee placement decisions. Information/training video tapes on these resource management products have been developed and disseminated. Improved resource management has assisted the Department in meeting or exceeding budget goals while providing offices with the resources required to transition to the reinvented HUD.

Summary

In 2 years, excellent progress has been made around the key management strategies that have guided HUD's internal review and assessment. As detailed in the examples above, HUD has built a management structure which updates its strategic vision and provides a foundation for optimal performance. HUD has implemented results-oriented management and accountability to measure and provide regular performance reports of our progress. HUD has improved and continues to develop better business processes to enable HUD to be more responsive and improve our service delivery system; and HUD is strengthening workforce skills and analytical competency so that our staff can adapt to changing institutional and customer needs.

These actions enable HUD to move closer to meeting our primary goal of serving the needs of America's families and communities, through our programs and services, in a responsive and timely manner.

Appendix
Clarification of OIG List of 240 HUD Programs

Active Programs (60): Active programs are those programs which are authorized and have major appropriations, and those which the Secretary deems critical to HUD's mission

I. Public and Indian Housing Capital Fund

PH/IH Development
PH/IH Amendments
PH Major Reconstruction
PH Severely Distressed Housing
PH/IH Modernization
PH Vacancy Reduction
Tenant Opportunity Program
Urban Youth Corps
Family Investment Centers
Youth Apprenticeship
PH Coordinators

II. Public and Indian Housing Operating Subsidies

PH/IH Operating Subsidies
Drug Elimination Grants
Youth Sports
PH Service Coordinators

III. Housing Certificates Fund

Section 8 Certificates
Section 8 Vouchers
Section 8 Contract Renewals
Section 8 Family Unification
Section 8 for Persons w/ Disabilities
Section 8 for Persons w/ AIDS
Section 8 for Homeless
Section 8 Opt-Outs
Section 8 Counseling
Section 8 Pension Fund Certificates
Section 8 Veterans Affairs Supportive Housing
Section 8 Headquarters Reserve
Lease Adjustments
Family Self - Sufficiency Coordinators

IV. Assisted Housing Fund

Flexible Subsidy
Title VI Preservation Program
Section 8 Property Disposition
Section 8 Loan Management Set-Aside
Elderly Housing Service Coordinators
Project-Based Service Coordinators
Congregate Housing Services

V. Community Opportunity Fund

CDBG
Economic Development Initiative
EZs/Economic Development Initiative
UDAG Recaptures
Youthbuild
Colonias
Early Childhood Development
Neighborhood Development
Community Adjustment Planning

VI. Affordable Housing Fund

HOME
National Homeownership Fund
Housing Counseling
Elderly Housing (S 202)
Housing for the Disabled (S 811)
HOPE 2
HOPE 3
Lead - Based Paint Hazard Reduction

VII. Homeless Assistance Fund

Shelter Plus Care
Section 8 SRO
Emergency Shelter Grants
Supportive Housing
Innovative Homeless Initiative
Rural Homeless Grant/Safe Havens

VIII. Housing Opportunities for Persons w/ AIDS

Housing Opportunities for Persons w/ AIDS

Active Programs II (115): This is an elaboration of the previously identified 60 active programs. This list includes small appropriated programs, assumed consolidations in FY 1995, suballocations within formula-driven grants, set-asides, eligible activities within programs, and simple accounting differences by the HUD IG (e.g. "PH/IH Development" is considered two separate programs by the IG). This list demonstrates all the program activities HUD will consolidate into the 7 performance-based funds in FY 1996.

I. Public and Indian Housing Capital Fund

PH Development
  Indian Housing Development (Fair Share)
  PH for Disabled Families
  IH Mutual Help Homeownership Opportunity
PH/IH Contract Amendments
PH Major Reconstruction
PH Revitalization of Severely Distressed Housing
PH/IH Modernization
  Comprehensive Grant Program
  Comprehensive Improvement Assistance
  IH Comp Grant
  IH CIAP
  Modernization Set-Asides
    CGP Emergency and Natural Disaster Reserve
    Earthquake Emergency Supplemental
    LBP Risk Assessment
    LBP Indemnification
    CGP Allocation from CGP Carry Over
    CIAP Allocation from CIAP Carry Over
PH Vacancy Reduction
PH Coordinators
Family Investment Centers
Youth Apprenticeship
Tenant Opportunity Program
Urban Youth Corps

Other Activities To Be Consolidated Under the Capital Fund
PH Demolition and Disposition
  IH Demo Dispo
Section 5(h) Homeownership
Youth Violence Prevention
PH Youth Development

II. Public and Indian Housing Operating Subsidies

PH/IH Operating Subsidies
Community Partnership Against Crime (COMPAC)
  Drug Elimination Grant
  Drug Information Clearinghouse
  Youth Sports
PH Service Coordinators

Other Activities To Be Consolidated Under Operating Subsidies:
PHMAP
Step-Up (administrative activity; no appropriation)
PH MINCS Demo

III. Housing Certificate Fund

Section 8 Housing Certificates
Section 8 Housing Vouchers
Section 8 Certificates for Persons w/ Disabilities
Section 8 Certificates for AIDS
Section 8 Certificates for Homelessness
Section 8 Pension Fund Certificates
Section 8 Veterans Affairs Supportive Housing
Section 8 Contract Renewals.
  Vouchers
  Certificates
Section 8 Family Unification/Foster Child Care
Section 8 PH Relocation/Opt - Outs:
  Certificates
  Vouchers
S 8 Contract Amend/Rental Adjustments
Section 8 Headquarters Reserve:
  S.8 Certificates Headquarters Reserve
  S 8 Vouchers Headquarters Reserve
  S 8 Certificates Litigation
  S 8 Vouchers Litigation
  Section 8 Cert./Vouchers FEMA Disaster Relief
  Section 8 Certificates for LA Earthquake
S 8 Counseling
Family Self - Sufficiency Coordinators

Other Activities To Be Consolidated Under the Housing Certificates Fund
Section 8 Existing Housing Contract
Portability Fees:
  S 8 Certificates Portability Fees
  S 8 Vouchers Portability Fees
  S 8 Cert Headquarters Reserve Portability Fees
  S 8 Vouchers Headquarters Reserve Portability Fees
Section 8 Homeownership Initiatives

IV. Assisted Housing Fund

Flexible Subsidy
Title VI Preservation Program
  S 8 Contract Renewals
Section 8 Property Disposition Set-Aside
Section 8 Loan Management Set-Aside

Elderly Housing Service Coordinators (Expanded 202 Service Coordinators)
Project - Based S 8 Service Coordinators
Congregate Housing Services

Other Activities To Be Consolidated Under the Fund.
Section 8 Property Disposition
Certificates
Vouchers

V. Community Opportunity Fund

CDBG:
Entitlement
Nonentitlement
Section 108 Loan Guarantees
Indian CDBG
Empowerment Zones/Enterprise Communities
Economic Development Initiative
EZs/Economic Development Initiative
LIFT
Community Viability Fund
UDAG Recaptures
Youthbuild
Special Purpose Grants
Colonias
PH Early Childhood Development.
Indian PH Early Childhood Development
Heinz Neighborhood Development Program
Community Adjustment Planning

VI. Affordable Housing Fund

HOME.
Local
States
Insular Areas
Indian HOME
National Homeownership Fund
Enterprise Zone Homeownership Opportunity
Housing Counseling.
Housing Counseling Services
Emergency Homeownership Counseling
Homeownership/Rental Counseling Train
Housing Counseling Assistance
Prepurchase/Foreclosure Prevention Counseling
Supportive Housing for the Elderly (S.202).
ECHO Housing for the Elderly
Supportive Housing for Disabled (S 811)
HOPE II Homeownership of MF Units
HOPE III Homeownership of SF Homes
Lead-Based Paint Hazard Reduction

VII. Homeless Assistance Fund

Shelter Plus Care
Section 8 Mod Rehab for SRO's
Emergency Shelter Grants
Supportive Housing
Innovative Homeless Initiative
Rural Homeless Grants/Safe Havens for Homeless Individuals

VIII. Housing Opportunities for Persons w/ AIDS

Housing Opportunities for Persons w/ AIDS

Ongoing Functions (10): HUD will continue several set-asides within the performance-based funds in FY 1996 and beyond.

Public and Indian Housing Capital Fund

Indian Housing Development*
Tenant Opportunity Program*

Community Opportunity Fund

CDBG for Insular Areas
Historically Black Colleges/Universities
Joint Community Development

Affordable Housing Fund

Work Study Program
Community Outreach Partnership Centers
Lead-Based Paint Research and Development

Separate Appropriations

Indian Housing Loan Guarantees
Native American Finance Service Organization

* These are functions previously accounted for in the Active programs list

Inactive Programs (29): Inactive programs are those programs that have either been repealed or are authorized but are no longer appropriated. HUD has designated staff to continue the operations of some of these inactive programs in order to maintain existing housing developments. These programs do not generate new activities and are being phased out.

S 8 Mod Rehab Amendments
S 8 Mod Rehab (Sec Adjustments)
Section 8 Mod Rehab (other than SRO)
Section 8 Mod Rehab Disaster Assistance
Section 23 Conversions
S 202 Elderly/Handicapped Direct Loan Program
Section 23 Leased Housing (Adjustments)
Turnkey III
Rental Housing Assistance Fund
Rental Housing Assistance/Deep Subsidy
Rental Housing Assistance/State Agency Financed
Rent Supplement Program
MF Mortgage Insurance
Rental Housing
Rental on Cooperative Housing
Rental Projects
Rental Housing for the Elderly
Construction/Substantial Rehabilitation of Condos
Purchase of Fee-Simple Title from Lessors
Section 235 Homeownership Assistance
Section 236 Interest Reduction Program

The following have been repealed
Urban Development Action Grants (UDAG)
Land Development Program
Rental Housing Development (HoDAG)
Rental Rehabilitation Loan
Rental Rehabilitation Grant
Urban Homesteading
Nehemiah Housing Opportunity Grants
Supplemental Assistance for Homeless Facilities
Assistance for Solar Conservation Improvements

Proposed Program Terminations (37): HUD proposes to repeal or consider for repeal the following program activities because they are no longer active, no longer appropriated, duplicative, or have been replaced with new initiatives.

III HOPE I/Section 5(h) Housing Replacement
HOPE I S 5(h) Housing Replacement
HOPE for PIH Homeownership
Choice in PH Management
Choice in PH Management TA
Moving to Opportunity/Counseling Set - Aside
MTO Section 8 Cert /Vouchers
MTO for Fair Housing Demo
PH One Stop Perinatal Services Demo
Section 8 Rental Certs WDC Project

Elderly Housing Supportive Service Program
HOPE for Elderly Independence
HOPE for Elderly Independence (Section 8 Certificates)
HOPE for Elderly Independence (Section 8 Vouchers)
HOPE for Elderly Indep Service Coordinators

Home Mortgage Insurance
for Outlying Areas
for Homes in Urban Renewal Areas
for Service Members
for Experimental Housing
in Military Impacted Areas
for Manufactured Home Parks
Mortgage Insurance: Group Practice Facilities
MF Housing and Investment Strategies/Process
Energy Efficiency Demonstration (NAHA 1990, S. 961)
Energy Efficiency Demonstration (NAHA 1990, S 523)
Homeownership Demo: Omaha, Nebraska
Solar Assistance Financing Entity
National Cities in Schools
New Towns Demo for Relief in L.A.
PH Community Development — Disaster Relief Assistance
Community Investment Corp. Demo:
Capital Assistance
Development Services/TA
Training Program
Enterprise Zone Development
College Housing Grants
Regulatory Barrier Removal Program
Community Housing Development Resource Board

FHA Insurance Authorities/GNMA (31): HUD does not define FHA mortgage insurance authorities as self-standing programs with individual appropriations and administering staff. HUD will consolidate the following insurance activities into two basic FHA insurance authorities. FHA Single Family Insurance and FHA Multifamily Insurance. GNMA will continue to securitize FHA loans.

FHA Funds: Single - Family Insurance

Home Mortgage Insurance (basic)
Home Mortgage Insurance for Disaster Victims
Rehabilitation Home Mortgage Insurance
SF Cooperative Program
Purchase of Coop. Housing Units through Coop. Mortgage Project Mortgage
Home Mortgage Insurance for Low-Mod. Income Families
Home Mortgage Insurance for Condominium Units
Refinancing of Section 235 Mortgages
Home Mortgage Insurance — Special Credit Risks
Misc. Housing Insurance (in Older Declining Areas)
Graduated Payment Mortgages
Growing Equity Mortgages
Adjustable Rate Mortgages
SF Mortgage Insurance on Hawaiian Home Lands
SF Mortgage Insur. on Indian Reservations

FHA Funds: Multifamily Insurance

MF Mortgage Insurance:
- Cooperative Projects
- Purchase of Refinancing of Existing MF Hsg. Proj. for SRO's
- Rental Housing in Urban Renewal Areas
- 2-Year Operating Loss Loans
- Equity Loans
- Nursing Homes
- Hospitals

Supplemental Loan Insurance — MF Rental Housing

The following will also be consolidated into two FHA Funds:
Manufactured Home Loan Insurance
Property Improvement Home Insurance
Home Equity Conversion Mort. Ins. Demo
FHA MF Mortgage Credit Demo
Direct Endorsement Program/Process (regulatory)

GNMA

Mortgage-Backed Securities Program
GNMA REMICs

Regulatory Authorities (17): These are statutory authorities which are not programs themselves but are either program requirements for HUD and HUD grantees, HUD enforcement activities, or authorities for activities. HUD intends to consolidate the 17 existing regulatory authorities into 9 authorities.

Fair Housing Enforcement
(includes the following consolidations)
- Fair Housing Initiatives Program:
  - Administrative Enforcement Initiative
  - Private Enforcement Initiative
  - Organization Capacity-Building Initiative
  - Education and Outreach
- Fair Housing Assistance Program
- Fair Housing Substantial Equivalency Cert.
- HUD-Assisted EO Enforcement Program
- Voluntary Compliance Program

Family Self-Sufficiency
Manufactured Home Inspection/Monitoring (Enforcement)
Interstate Land Sales (Protection/Enforcement)
RESPA
CHAS
Economic Opportunities for Low - Income Persons (Section 3):
- Section 3 TA (administrative activity; no appropriation)

Title X Lead Hazard Reduction Enforcement
GSE Oversight

Support Functions (15): HUD will continue to support technical assistance and training programs in each of the performance-based funds in FY 1996 and beyond.

Modernization TA
PH Development TA
TA and Training for Public and Indian Housing Crime Prevention Through Environmental Design
Indian Housing TA/Info. Clearinghouse
TA and Training for Resident Patrols
Prepayment Preservation TA/Capacity Bldg.
State CDBG TA Set - Aside
TA for State/Local Agencies
Integrated Data Base/Computer Mapping
HOME CHDO TA
TA for State/Local Housing Strategies
Youthbuild Management and TA
Youth Leadership Development:
- TA and training for PHA staff

Economic Development Training
Lead-Based Paint TA and Capacity Bldg.

Other Program Clarifications

Inapplicable Activities (1): The Neighborhood Reinvestment Corporation, an independent agency, was identified as a HUD program/function HUD has no program responsibilities for the NRC

Neighborhood Reinvestment Corporation

Programs/Regulatory Activities HUD Has Identified Which Are Not on the IG List (-13)

Community Adjustment Planning
LIFT
Economic Development Initiative
EZ√Economic Development Initiative
Community Viability Fund
UDAG Recaptures
Native American Finance Service Organization
COMPAC
Section 8 Counseling
Section 8 Certificates for Homelessness
Section 8 Certificates for Homeless Persons w/ AIDS
Title X Lead Hazard Reduction Enforcement
GSE Oversight

From Reinvention to Action:

15 Ways the New HUD Helps People

In March 1995 the U.S. Department of Housing and Urban Development sent to Congress a comprehensive plan to reinvent the agency, its programs, and its approach to people and the communities in which they live. This plan has three major components:

- Consolidation of programs into three major performance funds -- Affordable Housing Fund, Community Opportunity Fund, and Housing Certificates Fund;

- Transformation of public housing and the creation of choice and mobility for families; and

- Formation of a government-owned federal housing insurance corporation that will join with public and private partners to help achieve an all-time high homeownership rate.

Following are just some of the concrete ways this reinvention helps people.

Program Consolidation

1. Program Consolidation: Hindrance to Help

Critics often say HUD has an overwhelming number of programs, with estimates ranging from 60 to 240, that have done little to help address community needs in a comprehensive way. HUD's reinvention plan simplifies programs while providing greater local flexibility.

HUD will consolidate 60 active programs into three new performance-based funds; phase out 29 inactive programs; terminate 37 duplicative or obsolete programs; and consolidate 16 technical assistance programs into a simplified support system for each new fund.

No longer will Philadelphia, a leader in coordinating city, nonprofit and neighborhood groups to address housing and community development needs, have to spend unnecessary time applying for multiple grants throughout the year, filling out paperwork, administering disparate programs, and attempting to plan around non-guaranteed sources of federal funds. In short, Philadelphia and other cities will be able to concentrate on the real issues at hand -- solving the problems of communities -- not the pursuit of money. John Kromer, Director of Philadelphia's Office of Housing and Community Development, looks forward to these changes and what they can do for Philadelphia's efforts to address community needs. For information, contact John Kromer, 215-686-9750.

2. Community-Based Consolidated Planning: Simplicity and Flexibility

Today communities must submit many applications and plans to receive community development, homeless, and economic development funds from HUD. For too long, the sheer number of HUD programs has stifled innovation and creativity within communities.

The new Consolidated Plan condenses 12 separate HUD programs and applications into one application and one plan. This greatly simplifies the process for communities and reduces lengthy and burdensome paperwork requirements. Communities will now be able to develop a vision and strategy to address locally identified needs. In addition, HUD has developed innovative computer software with mapping capabilities to enable communities to develop and submit their Consolidated Plans to HUD on disk. Citizen participation will be significantly enhanced through innovative technology such as the InterNet, satellite television networks, and interactive cable television.

Gary, Indiana, recently submitted a Consolidated Plan that outlines the city's housing needs, a continuum of care approach to address homelessness, economic development strategies undertaken by nonprofits, and a comprehensive medical services program for at-risk populations. Gary's Consolidated Plan is innovative, streamlined and flexible.

3. Community Partnerships: Nonprofits Making A Real Difference

Over 3,000 nonprofit community development corporations in cities and rural communities across America are producing housing and providing services for low- and moderate-income Americans. Community development corporations have created thousands of units of affordable housing and have initiated innovative economic development projects.

HUD wants to build on the success of nonprofit community development by directing 30 percent of the Affordable Housing Fund to the nonprofit community development sector. This represents an unprecedented resource commitment to nonprofits at the community level.

In a community such as Chattanooga, one community-based organization has made a real difference. Chattanooga Neighborhood Enterprise (CNE) has helped more than 3,000 families move into decent and affordable housing since the organization was founded in 1986. In the past year alone, 342 families became homeowners and 146 homebuyers renovated their homes. For information, contact Leigh Ferguson, CNE Executive Director, 615-265-4114.

4. Rewarding Performance: Bonus Funds for Communities

The essence of President Clinton's new approach to government borrows from a concept long embraced by the private sector: rewarding good performance. HUD will reward excellence in management in the Community Opportunity Fund through a proposed bonus pool for good performers in the community development block grant program. This bonus pool will give good performers the opportunity to compete for additional funds to develop large-scale job creation projects in distressed areas and address problems such as environmentally contaminated land known as brownfields.

The City of Louisville, for example, has been contending with significant environmental contamination that has hampered housing development and economic development efforts. With a performance bonus pool, Louisville could compete for funds to begin to address brownfield problems. For information, contact Caroline Gatz, Special Assistant to the Mayor, 502-574-4210

5. Homeless Consolidation: Implementing Continuum of Care

Reducing homelessness is HUD's number one priority. Until now, specialized homeless programs with separate program rules and narrow regulations have encumbered local governments and community-based nonprofits that seek to provide comprehensive services for this needy population.

But now, HUD's proposal will consolidate HUD's six McKinney homeless programs into a single Homeless Assistance Fund. This consolidation will enable localities to shape a comprehensive, coordinated "continuum of care." Funds will be allocated to communities through a need-based formula.

Unity, a unique partnership organization in New Orleans, is implementing the continuum of care strategy by providing a seamless web of housing, services, and job training. Unity brings together the private sector, the federal and local government, and the nonprofit sector in the financing and delivery of services to the homeless. Executive Director Peg Reese praises HUD's efforts in developing the continuum of care: " . . . the federal government, under Secretary Cisneros' leadership, has given communities the tools to design and complete their own continuum of care strategy. Since the phenomena of homelessness began a decade ago, the support that we have gotten from this Department has made more impact than at any other time." For information, contact Margaret Reese, Executive Director, 504-821-4496.

6. Native American Reforms: Increasing Opportunity

Native American must content with some of the worst housing conditions in America. Unemployment rates are high and jobs are rare. Native American communities also have trouble attracting private

capital because of the lack of modern financial and legal systems, and physical infrastructure challenges.

HUD's reinvention plan will consolidate all Native American programs into one office. Set asides under the Community Opportunity Fund and Affordable Housing Fund are increased from 1 percent in FY 1995 to 1.5 percent in FY 1996, which means $172 million more for Native American housing production and community development. HUD has also proposed a 1.5 percent set-aside in each fund for Native American technical assistance. To increase homeownership and economic development in Native American communities, HUD will continue the successful Loan Guarantee program and encourage the development of a Native American Finance Service Organization (NAFSO) to provide technical assistance to create lending institutions.

These program reforms will provide extensive benefits for Native American nations, such as the Oglala Sioux Reservation, in South Dakota. The Oglala Sioux will have the ability to develop a Consolidated Plan for comprehensive housing, community infrastructure and economic development needs. They will have the flexibility to implement the tenets of self-governance by developing a program to use grant dollars on priorities the Nation deems most important, without a great deal of federal oversight and interference. Paul Iron Cloud, Executive Director of the Oglala Sioux Indian Housing Authority, sees HUD's reinvention as a dynamic opportunity for advancing housing and community development throughout Indian Country. For information, contact Paul Iron Cloud, 605-867-5161.

Transformation of Public Housing

7. Opportunities for Working Poor: Helping People Help Themselves

Public housing was intended to be transitional housing, not permanent housing for America's poorest families. HUD is returning to the original notion of public housing -- a first step on the ladder of self-sufficiency.

HUD's new proposal will allow PHAs to issue up to half their certificates to working families and those preparing to enter the workforce.

Many cities, including New York City, have instituted a policy to accept a certain percentage of working families into public housing. Chairman Reuben Franco of the New York City Housing Authority says residents of public housing should reflect residents of the community at large. He believes there should be a healthy economic mix of working and non-working families to add vitality to a community. For information, contact Reuben Franco, 212-306-3000.

8. Making Work Pay: Ceiling Rents and Removing Obstacles to Work

Currently public housing residents frequently are discouraged from working, because HUD regulations require that they pay 30 percent of their income in rent despite the value of the apartment. Residents who do work often experience dramatic rent increases, a difficult problem given the modest nature of their discretionary income. In addition, as their rent increases dramatically with employment, residents incur new expenses -- for child care, clothing and transportation to work. Although their living conditions have not improved, they are left in financially worse shape than when they were unemployed. Some low-income married residents report that spouses live separately when one obtains temporary work, because the rent rises sharply, even though the job is only short term.

Changing the rent rules so that there is a maximum rent that is phased in, rather than a dramatic increase at one time when a resident finds a job, in addition to providing preferences for working families, will encourage working residents to remain in good public housing. This will increase the occupancy of public housing developments by people with a broader range of incomes, which every housing expert confirms is essential to effective housing management. In addition, working families can begin to save money so they can progress to private housing and homeownership and in the meantime provide the needed role models that many public housing communities are missing today.

For information, contact John Hiscox, director of the Macon Housing Authority, 912-752-5070, a leading expert and proponent of public housing rent reform.

9. Empowering Residents to Control Their Destiny: Resident Management

HUD recognizes that the problems of public housing can only be solved with the active involvement and commitment of the residents. A major development of recent years has been HUD's award of grants to more than 300 resident councils for resident activities and organizing.

Working with the new HUD, residents will play an integral role in management. Residents will take responsibility for how their community operates and have a stake in its success -- not just for themselves, but for their neighbors. They will help decide the needs of the community and help set priorities for limited resources. Not only will residents hold the housing authority accountable, but each other as well. Resident councils will have the right to purchase units. And, HUD will work with resident groups to launch a program to find jobs and community service opportunities for unemployed residents.

At Abbottsford Homes in Philadelphia, resident management has helped in addressing the physical upkeep of the property. The grounds are cleaner and most of the graffiti has been removed. Rent collection has improved. Vacancies have been reduced, and the crime rate has dropped by 30 percent.

10. Public Housing Capital Fund: Maximum Flexibility To Improve Housing

Currently housing authorities are required to use one pot of money to repair obsolete buildings and another pot to demolish and rebuild public housing. Because of the unavailability of funds to construct new public housing, housing authorities frequently have no choice but to renovate buildings that because of poor designs and age should be demolished and replaced. The result is money now earmarked for rehabilitation, called modernization funds, is spent to little avail.

In the era of reinvention, HUD's proposed consolidation of all capital funds for housing authorities will enable cities to make appropriate decisions at the community level. This new policy will enable cities to demolish and replace buildings that are unfit for habitation. The flexibility this fund will provide will save money and time.

Rick Gentry of the Richmond Redevelopment and Housing Authority supports any increase in flexibility for housing authorities to deal with particular problems in locally determined ways, including demolition and replacement. For information, contact Rick Gentry, 804-780-4246.

11. End One-For-One Replacement: Eliminating Burdensome Federal Regulations

In Chicago, Philadelphia, Baltimore, and many other cities, a significant amount of uninhabitable

housing is draining the resources of housing authorities. Under the one-for-one rule instituted in 1987, every unit of housing to be torn down must be replaced by a new housing unit. Since development funds are very scarce and communities confront local obstacles, such as zoning, land costs and local opposition, they are not able to build new units. Therefore, cities are left with thousands of vacant, obsolete developments that blight neighborhoods.

The key to the new policy is not unit-by-unit replacement but a thoughtful plan to house residents relying on certificates and vouchers. The result will be new housing for residents and greater flexibility for housing authorities in dealing with older developments.

Commissioner Daniel Henson of the Baltimore City Housing Authority has been trying for eight years to demolish the abandoned Fairfield Public housing development. With the one-for-one rule, this has proven to be an impossible task. Commissioner Henson favors using a voucher and certificate system for residents. For information, contact Daniel Henson, 410-396-3232.

Choice and Mobility For Families

12. Certificates: Maximizing Choices For Families

Today's federal rental assistance system too often ignores the dignity of families and prevents people from freely choosing where to live. HUD's proposal will offer Americans in need of the government's housing assistance the same choice and opportunity as all other Americans.

To increase the number of families moving out of severely distressed areas, HUD will authorize cities to use a specified portion of certificates to enable families with children to move from high-poverty to low-poverty areas. Families receiving these certificates will also receive mobility counseling and search assistance. A new emphasis in the Housing Certificates Fund will be HUD's proposal to use a certificate to purchase a home. For families prepared to assume the responsibilities of owning a home, certificates -- traditionally available to pay rent -- can be used for mortgage payments. This initiative provides a great opportunity for families with modest but growing incomes to own their own home.

Andrea Duncan of the Louisville Housing Authority has converted public housing units into condominiums by using HUD funds to rehabilitate and transform units to be sold at affordable prices. So far, 365 renters have become homeowners. For information, contact Andrew Duncan, 502-574-3400.

13. Eliminate "Take One, Take All": Making Certificates Attractive to Landlords

The old way of doing business -- "take one, take all" -- forced landlords to accept all qualified recipients in their rental properties once they accepted one Section 8 tenant. Many landlords were reluctant to join the program because they feared their apartment buildings would lose their mix of renters with varying incomes and would assume the worst characteristics associated with public housing.

Under new guidelines, landlords will be able to accept as many or as few certificate holders as they want. The result will be better management of buildings and a greater universe of landlords willing to participate in the Housing Certificate program.

Following the Northridge earthquake in January 1994, HUD waived the "take one, take all" provision. This flexibility for landlords helped more than 12,000 families move into apartments within several months. It proved to HUD that flexibility matters to landlords because so many more landlords were willing to come to the Section 8 program. For information, contact Steve Renahan of the Housing Authority of Los Angeles, 213-252-2570.

Government-Owned FHA

14. Homeownership: Realizing the American Dream

Every person needs a place to live, to raise a family, and to develop a sense of personal financial security. For most Americans, this "American Dream" is just a dream because vast numbers of households cannot afford decent housing. HUD's unprecedented effort to generate more homeowners than ever before is the purpose and driving force behind the Federal Housing Corporation (FHC), HUD's new vision of the FHA.

HUD's proposed government-owned insurance company, combined with public and private sector partners, will help achieve an all-time high homeownership rate by cutting the amount of down payments for homebuyers, simplifying the process of buying a home, opening new markets, including underserved populations, and conducting education and outreach for millions who don't own a home.

Lydia Maynard, a single mother of three from Washington, D.C., was able to buy an FHA-owned home because this nation has remained committed to a federal role in homeownership. Lydia, a secretary at the Department of Agriculture for nine years, resided in assisted housing prior to the purchase of this home. Using an FHA program that provides additional monies for the rehabilitation of the property, Lydia Maynard has increased the value of her property by over $20,000. The Performance Mortgage Company is one of many partners that has joined HUD in the recommitment to the American Dream. Performance Mortgage helped Lydia purchase her home. Contact Performance Mortgage, 410-825-5700.

15. Reforming Government-Assisted Rental Housing: Saving Taxpayers Money

Taxpayers should not be subsidizing rents that are inflated far over the market price. But, in many instances, this is just what is happening today. Some 75 percent of the rents paid to landlords of subsidized multifamily units exceed the local Fair Market Rents, some by as much as 75 percent. HUD knows that subsidizing rents "above the market" does not necessarily create better living environments, it only costs taxpayers more money.

Therefore, HUD proposes to reduce the debt on the HUD-insured developments in its FHA inventory at a level that will permit the property to operate in the market with a reduced subsidy, or without any subsidy at all. This will save taxpayers billions of dollars.

The situation at Westview Towers in North Bergen Township, New Jersey, is a typical example of this phenomenon. According to HUD's estimates, the rents at Westview Towers are 30 percent higher than market rents. When the Section 8 contract expires in April 1996, the owner understands that under HUD's multifamily restructuring proposal, subsidy income to his development will decrease by over $600,000 per year. For Winchester Towers to remain viable, the first mortgage on this property must be reduced. HUD's proposal will do this.

REINVENTION OF HUD AND REDIRECTION OF HOUSING POLICY

THURSDAY, APRIL 27, 1995

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING OPPORTUNITY AND
COMMUNITY DEVELOPMENT, AND
SUBCOMMITTEE ON HUD OVERSIGHT AND STRUCTURE,
Washington, DC.

The Subcommittees met at 9:35 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Connie Mack (Chairman of the Subcommittee on Housing Opportunity and Community Development) and Senator Lauch Faircloth (Chairman of the Subcommittee on HUD Oversight and Structure) presiding.

OPENING STATEMENT OF SENATOR MACK

Senator MACK. I call the meeting to order. I suspect that some of my colleagues will be along in a little bit as the morning proceeds.

Good morning and welcome to the third in a series of Housing Subcommittee hearings focused on the reorganization of HUD and the reorganization of Housing and Community Development policy.

Today is a continuation of hearings to examine the mission, management, and programs of HUD and to explore the various proposals to restructure public housing and consolidate and streamline housing and community development programs.

The first part of this hearing will focus on public housing reform. Public housing is home to 1.4 million American families. Much of it is good housing.

Unfortunately, some public housing, particularly in major urban areas, is in deplorable condition.

Despite a 60-year, multibillion dollar commitment by the Federal Government, too many public housing developments have become havens for crime, drug abuse, and islands for welfare dependency, hopelessness and helplessness.

Public housing should once again become a rung on the ladder to self-sufficiency, not permanent shelters for generations of welfare dependent families.

As we look at ways to restructure the delivery of housing programs and reform our welfare system, the transformation of public housing may be our highest priority.

We need to devise strategies to end Federal requirements that effectively warehouse the poorest of families in public housing, and discourage them from becoming productive and self-reliant citizens.

We look forward to the ideas of our panelists, who have worked or lived in public housing, on ways to reform the system to provide greater choice to residents and incentives to become economically independent and self-sufficient, and to provide public housing authorities with the flexibility they need to manage public housing developments more effectively.

Today's hearing will also focus on proposals to consolidate and streamline HUD programs. We live in an era of diminishing budget resources and lingering questions about HUD's capacity to carry out its mission.

We therefore must explore ways in which housing and community development programs can be reconfigured to accomplish the Department's mission in a more efficient and effective way.

This will require providing maximum flexibility to States and localities to devise programs tailored to their needs.

We'll be interested in hearing the views of our witnesses, who represent various levels of Government and community-based non-profits, about what role their organizations may play in carrying out housing and community development policies in a restructured and consolidated program environment.

I'm pleased to welcome these distinguished panelists, which include experts in the field of public housing, as well as representatives from State and local governments and community-based non-profit organizations.

I hope today's hearing will provide us with some innovative ideas and solutions to problems facing communities and families.

I'm convinced that any solution must seek to empower the people served by these programs.

We look forward to your thoughts about how HUD programs can be consolidated and streamlined to serve American families more efficiently and effectively.

For purposes of today's hearings, we have divided the witnesses into three panels.

The first panel will begin with Steve Bartlett, who has been actively involved in the housing debate, both as a former member of the Congress, and as the mayor of Dallas, TX.

Our second panel will focus on public housing reform and will include a distinguished panel of public housing officials. Rick Gentry from the Richmond Redevelopment and Housing Authority. Audley Evans from the city of Tampa Housing Authority. We will also hear from Reverend Willie Carter, a resident leader from the Hunter's View Public Housing Development in San Francisco.

Our third panel includes two panelists presenting State views. Shirley Dykshoorn from the Office of Intergovernmental Assistance for the State of North Dakota and James Logue from the Michigan State Housing Development Authority.

We'll also hear from individuals representing local community-based non-profit organizations. Mr. William Frey from the Enterprise Foundation's New York City office and Danette Jones from the Madison Park Development Corporation in Boston.

We wish to thank all the witnesses here today for their time, interest and willingness to share their views on the future of HUD and housing and community development policy.

Before I call on our first witness, let me add one personal note.

I know that HUD's field office in Oklahoma City was tragically affected by last week's bombing and that many HUD employees in that office were killed, and some remain missing.

The prayers of this Subcommittee are with their families and the HUD family as well, both in its headquarters and in Oklahoma in this time of great trial.

Steve, again, I want to extend a personal welcome to you, and I appreciate your willingness to come before the Subcommittee today and express your views.

I remember when we came into the Congress together back in 1982, both of us freshmen Congressmen, and I was and have continued to be impressed with both your knowledge and your leadership in many areas, but in particular in the field of housing.

You were one of those, again, when I first arrived here, who made vocal and impassioned statements about the need to reform HUD and to provide greater opportunities to America's families.

With that background, it is a delight to see you here before the Subcommittee. I look forward to your testimony.

STATEMENT OF STEVE BARTLETT, MAYOR, CITY OF DALLAS, TX; FORMER MEMBER OF CONGRESS

Mayor BARTLETT. Thank you, Mr. Chairman.

Twelve years later, it appears that we're about to do that, to make some major reforms and restructuring.

Mr. Chairman, it's awfully good to see you and likewise, you and I have worked together through the years, both in the Senate and the House, and as mayor, I very much admire and appreciate your leadership and your willingness to tackle this rather difficult subject that has not been successfully tackled in the halls of Congress for some 20 years.

Mr. Chairman, I've submitted written testimony that I assume would be put into the record, and I would like to make one correction to that, though. Upon reviewing my testimony and rethinking it, the parts of the testimony on page two that imply or leave the impression that I think that performance-based measures actually can work, as I thought about that, I can't think of a way in which they can work.

So I'd like to delete that portion. I think that was being overly generous to the idea that a new set of regulations would be successful.

Mr. Chairman, when Secretary Cisneros proposed his rather dramatic and positive restructuring of HUD, I was, at the time, enthusiastic about that and remain so to this day. As I've thought about it, though, and reflected on two changes since January, I've altered my opinion somewhat.

No. 1, the world has changed. The political landscape has changed, and as dramatic as these reforms for the HUD reinvention appeared in January, given the light of the new political realities in the United States as a whole, and in Congress, it seems to me that this Blueprint can move much more dramatically than even this Blueprint does.

This was the most dramatic direction that I had seen to date.

No. 2, many of the principles that Secretary Cisneros articulated in his Blueprint, downsizing, devolution, and block grants, all those

principles are positive, but many of those principles got lost in the details of the actual Blueprint.

So in some ways, the actual Blueprint came out too little too late and should be used as a base to start, but not as a final end product.

Now let me give you a couple of examples to that.

For example, good words throughout, and the Secretary clearly believes them on page 3 and others on home ownership, and articulates all the reasons why home ownership opportunities for low-income families are positive and need to be put in. But not a single home ownership proposal, and in the entirety of HUD, the proposals are not redirected towards home ownership.

Similarly, the concept of empowering tenants in public housing with their own tenant-based vouchers or certificates are not implemented until the third phase, way down the road. And that tenant-based empowerment could be done and should be done in the first phase.

My recommendations to the Congress, based on both Congressional experience and city experience, are as follows:

One is adopt three overriding principles to HUD reinvention.

Those would be:

No. 1, empower the residents themselves, through downsizing and streamlining, voucherizing and privatizing of public housing.

No. 2, emphasize home ownership opportunities at all income levels in every single program.

No. 3, is progress with the devolution of power, and that is put the decisionmaking in housing in the hands of local governments, particularly cities, as close to a block grants to the cities or tax base relief to the cities as you can get.

The test in Congress then is to force a deliberation so that every phase, every page, every section, every paragraph, every amendment in the restructuring and reinvention of HUD meets those principles.

You and I have been here long enough to know that what happens is that every Senator and every Congressman comes in with a different idea or some little tweak. Then when you tweak HUD as much as it's been tweaked, you end up not abiding by the principles.

Mr. Chairman, I would recommend that both in your drafting of the reinvention of HUD and then in considering amendments, that you test every amendment by, does it accomplish the principles as opposed to is it just sort of a neat idea that somebody came up with.

In walking through the reinvention, I'd offer the following observations. One is the block grant approach is the right approach. The Secretary's proposals for the three block grants or four, but the three big ones of community opportunities, affordable housing, and tenant-based assistance, seems to me to make some sense actually. But whether it's 60 programs into four, or 240 into three is less important than a wholesale consolidation.

Forget performance-based measures which is just simply a new term for mandates and regulations. If you're going to block, just block it and put it in a block grant.

When you get all done, I would suggest that you step back, and you will still have too many regulations and mandates left over in all phases of the final block grants.

One way to get at that would be to designate a mandate or a regulatory commission and a sunset for all HUD regulations, all housing regulations and all mandates.

So pick a date, whether it's 18 months or 3 years, at the end of which all of those left over regulations would expire unless reenacted and reinforced by the Congress.

Now there are basically three models to a block grant that you can follow. Any of these are acceptable.

One is the classic community development block grant, which is now well accepted. It has been streamlined in recent years, first under Secretary Kemp, then under Secretary Cisneros, and generally understood.

Cities submit a plan. Once HUD approves a plan, with a fair, minimum amount of paper work, and that didn't used to be the case but it has been in recent years, then the city proceeds on the plan and then reports on the plan.

Second is the welfare reform waiver process that has been successfully used in Wisconsin, among other States, and that is a city or a recipient of a block grant could apply for its own plan and waive all regulations or mandates with a comprehensive waiver with its own plan.

Third would be the classic, the purest form of block grant and that is a general revenue sharing sort of block grant in which a city is required to comply with civil rights laws, but other than that, the money goes to the city for their disposal.

Public housing areas, the goal is right, but I would move the three transition phases from three to one, and start by issuing a deed in fee simple of public housing to the local public housing authorities or to the city, and allow those authorities to operate it, to replace it, to demolish it, to sell it, or to do anything else they choose to do, that will provide housing assistance for the local community. And then convert the operating subsidies to vouchers.

Again, all of this is in the Secretary's plan, but it's phased over such a long period of time, I fear you'll never get there.

Convert the operating subsidies to vouchers, and let the tenants decide whether those public housing, those existing public housing units are good places to live, or whether they want to live somewhere else.

If indeed the tenants want to live somewhere else, then the Federal Government should not be in the plantation master mode of telling them they have to continue to live, and then do all that deed without regulations.

The one-for-one replacement ought to be abolished. Dallas, as you know, has a special one for one replacement in that we're not even allowed to do the replacement. We have some 2,500 vacant, dilapidated units under the Frost Leland Amendment, owned by the Federal Government that the Federal Government is not allowed to do anything other than to subsidize them standing there by special provision of Federal law, which we hope will be repealed one day for the benefit of the residents.

Second is the community development block grant, to be known as the community opportunity fund.

No. 1 is review the formula. The formula of distribution has not been looked at since 1977, and that formula has a very heavy, had been and has now a very heavy and unfair bias towards the older cities, without regard to the physical condition or the level of poverty.

You also ought to upgrade the 70/30 split. Now it's 70 percent local communities and 30 percent to the States, and make it at least an 80/20 if not a 90/10 split.

Senator MACK. Say that again for me?

Mayor BARTLETT. Eighty percent, 20; 80 percent for the cities, 20 percent for the States.

A house is in a place, it's in a neighborhood, it's in a city. Its location in a State is largely irrelevant.

No. 2, cities have developed housing programs through their neighborhoods and community development programs. States by and large have not.

So the cities, particularly the large cities, have a much greater sense and expertise for operating community development.

The HOME program would be converted into what's called the affordable housing fund.

A couple of suggestions on that.

No. 1, the HOME program is working pretty well now. It took a few years to get it started, as you know. You were one of the authors of it in the Congress originally. I would eliminate the reference to special populations.

Local officials are elected by the same people that elect Senators and Congressmen, and special populations have the same ability to articulate their access to that funds at the local level as at the Congressional level.

One last remark, Mr. Chairman, if I could take an extra minute, on enterprise zones.

Enterprise, if this Committee, working with the other Committees through the Senate, could reinstate the original concept of enterprise zones, it would be the single most significant thing that you could do in community development and in housing in our Nation's cities.

The current empowerment zones and enterprise communities have no similarity to the original enterprise zone concept at all, none, zero, zip. Enterprise zones were designed to reduce taxes in distressed areas of poverty.

The empowerment zone and enterprise communities are designed to focus Federal grants on an area of poverty that cities could apply for; no relation.

Enterprise zones have a proven model of success in states and cities. The city of Dallas alone, in the last 4 years, we designated 15 percent of our land area in our distressed areas as enterprise zones. And we offered to reduce or eliminate city property taxes, the smallest expense an employer could pay. We offered to eliminate or reduce those property taxes for new employers coming in in the enterprise zone.

As a result of that small reduction, 41 new employers, 7,500 new jobs, and a $200 million investment.

Now consider what that would have looked like, had we been able to say zero property taxes or zero payroll taxes in those same areas that don't apply to other areas.

So my recommendation is twofold:

First, either take all currently designated enterprise zones and simply eliminate the grants and convert them into a zero capital gains or zero payroll taxes.

Or, if the Congress could actually be pure on it, simply have it self-designated through pockets of poverty, through the census tract legislation.

Mr. Chairman, I had some other things.

Repeal the one-for-one replacement, repeal Davis Bacon. We just used some HOME funds, for example. Repeal Davis Bacon at least as regards housing programs. It's not relevant, it only gets in the way.

We just built a subdivision——

Senator MACK. Say that for me again.

Mayor BARTLETT. Davis-Bacon has no relationship to housing, but it is imposed on housing, OK? Union labor does not typically build a housing or subdivisions. We are participating in the development of a subdivision, using HOME money, in which HOME money put in the sidewalks and the streets and some of the infrastructure, OK.

But most of the money comes from the lenders, from the builders, from the home buyers themselves in a subdivision of $45,000 homes. That part of town hasn't had a new house built in 15 years.

Of a $45,000 house, $900 of that cost of each lot was the result of Davis Bacon. Same lot, same lot size, same house size, but these home buyers end up having to pay an additional 900 bucks just for the privilege of having the Federal, of having HOME money as the infrastructure.

It was such a burden actually that we considered not using HOME money at all because that extra $900 was almost not worth it. So I would invite that.

In FHA, don't go with the Government corporation. Privatize it. The Fannie Mae model works exceedingly well. Fannie Mae may be the most successful housing program in American today. It's a Government-chartered corporation, so privatizing FHA is what makes the most sense.

Mr. Chairman, I appreciate the chance to testify.

Senator MACK. Well, again, Steve, I appreciate your comments this morning, and frankly you probably have answered most of the questions that I prepared to ask you, but let me touch on a few.

In your comments, I think you pretty much have already made this point, but I gather that you feel that local governments are much better suited to administer housing and community development block grants?

Mayor BARTLETT. Than either the Feds or States. Yes, the States, you can make a strong case for States having a block grant on welfare assistance because the States are well-equipped to do that with the transfer programs.

But in housing circles, the local communities, cities, and redevelopment authorities are the ones that are on the front lines and

have been for 20 years, and States are generally not equipped to set up housing programs.

If they do, the States would tend to drive housing towards the suburbs as opposed to the inner-city. No. 1, because it's easier, it's easier to build on an empty piece of ground than redeveloping the inner cities. It's easier, you get more production. No. 2, it's better politically because unfortunately in this country, people in the suburbs tend to vote in higher proportions than people in the inner cities.

So if you send the block grants to the States, you will have results that you won't like. You'll have the continued deterioration of the inner cities, central cities.

Senator MACK. Let's just take a moment, though, to— what do those on the other side of this issue say? I mean, what's their strongest argument about why it ought to go to the States?

Mayor BARTLETT. Their argument, as I understand it, is that they would extrapolate on the welfare reform side and say the States are operating welfare reform, so they ought to operate housing. And it's just simply an unrelated issue.

But I think that would be their argument, and as far as welfare or AFDC assistance kinds of programs, States operate Medicaid, States operate, either operate direct or through county hospitals, health care, AFDC, food stamps and other kinds of direct assistance.

But in the area of housing, housing and neighborhood redevelopment is very local, and States simply get in the way.

Senator MACK. Since you mentioned welfare, there has been some discussion about really kind of linking housing assistance and welfare reform.

Do you have some specific recommendations that you would propose combining the various forms of housing and welfare assistance?

Mayor BARTLETT. I would keep the two separate. While housing assistance does have one notion of it that is means tested, people live in a house and that's not fungible. You don't, you can take your food stamps or your AFDC or your cash and you can use it to buy a lot of other things, but once you put down a mortgage on a house, or you pay your rent, that is a place, that is your home, that's No. 1.

No. 2, that house is in a neighborhood and what happens in the neighborhood has more to do with your quality of life than anything else in your life. And if you convert it strictly to a welfare assistance kind of program, or money that goes to that particular person, you haven't changed the neighborhood at all.

So my sense is combining it with cash payments and welfare assistance payments, while they are related, it's still apples and oranges.

Senator MACK. Well, some have suggested that there ought to be some kind of a time limit with respect to housing assistance.

As you know, today there's a great deal of discussion on the welfare side to a certain commitment time-wise, and after that, they're no longer entitled to it.

What's your reaction with respect to housing?

Mayor BARTLETT. There should be. In fact, I propose that in every session of Congress during the time I was in the Congress. The time limit is one that would have a dramatic positive impact on the residents themselves. Even more so, a time limit on Section 8 eligibility or affordable housing assistance, even more so than a time limit on AFDC or food stamp kinds of payments.

The reason is because if a resident goes into a public housing unit or into a Section 8 and knows that that voucher is only good for 2 years, or 5 years, and at that point, they have to start paying graduated market rent, that person will begin to readjust their life while using the housing assistance as more of a temporary assistance.

In fact, we have the reverse today, and that is we have a stipulation that as your income goes up, your rent goes up, and that causes people to hold their income down.

Now actually, there's a fairly easy way to do that. It doesn't have to be a Federal mandate. The easy way to do it would be to allow public housing authorities to establish a minimum rent after a year or 6 months or 18 months, to establish a minimum rent that has a graduated scale so that you say to someone, you pay 30 percent of your income, which is the current law, 30 percent of your income for rent, but after 2 years, you have to pay at least 100 bucks, or after a year. And after 2 years, you have to pay at least 200 bucks and so forth, until you get up to market rent.

Thus you push, gently ease people out of the golden handcuffs of assistance.

Congress doesn't have to actually mandate those time limits. If you allow public housing authorities the ability to set time limits, they will do it.

Senator MACK. Will they do it because it's in their self-interest to do it?

Mayor BARTLETT. If you make it that way. Now, I assume by that, by the way, the Congress would allow public housing authority to set the time limit, but to then recover the money that they save and put it back into other vouchers.

In the city of Dallas, we have some 7,500 vouchers. If we had a time limit, we could have 10,000 vouchers by recycling the same money.

Don't recapture the money back to the Federal Treasury because public housing authorities won't go through the grief in large part.

Senator MACK. Good point.

There's also been a lot of discussion, as you know, over these last several months about the possible elimination of HUD. And in going into a block granting and transferring oversight functions to Federal agencies and so forth.

I was just interested in what do you think about those proposals?

Mayor BARTLETT. Well, I have read those proposals and thought about it some, and I don't think it's a good idea. My sense is it's the programs themselves that are the problem, not whether it's in one agency or three agencies.

So, as I said earlier, I don't believe that the HUD programs ought to be consolidated into a State-run welfare agency, because they're not related and cities would just simply have another bu-

reaucracy to deal with. And the new bureaucracy would be actually amazingly less equipped than the current HUD.

The current HUD agencies, based on Secretary Kemp's reforms and now Secretary Cisneros' reforms, the current HUD are by and large cities are able to deal with it. There are all kinds of anomalies and regulations that tie us down, but at least it makes some sense.

Turn it over to the States and you have to start over.

In terms of abolishing HUD altogether, you have too much money going out the door that you could abolish the agency, so streamline it and downsize it, but if you abolish it, you'd make it harder to deal with rather than easier.

Senator MACK. Again, I think you may have touched on this, but I want to just pursue it.

We're talking about the consolidation of programs, the block granting. Of course, you've suggested that 80 percent go to local communities, and 20 to the States.

There has been I think, there've been a number of questions and concerns raised about the capacity of staff resources at the local level to carry out these programs.

Do you consider that to be a legitimate concern?

Again, the thought of, you know, kind of saying, all right, we're going to send all this money down to !ocal communities or even to States, for that matter. I should suspect that some States are much more equipped, much better equipped to deal with housing issues than other States, and the same thing with local communities.

What kind of oversight, or what kind of, I mean, on one hand, should we just turn the entire amount of money over with no kind of management requirements?

I mean, how do we balance that, I guess is what I'm asking.

Mayor BARTLETT. The best way to balance here, or the least radical would be to turn it over to the cities, particularly the larger cities for an eligible list of activities. Require the city to produce a plan similar to CDBG or the program that we got started in the late 1980's, comprehensive modernization.

Where the city or the PHA produces a plan for what they are going to do for those eligible activities. And then reports every year on their progress to their own plan.

Now that's different from a performance based measure. That is a block grant with a plan, and in essence, they are reporting to their own citizens, as well as to HUD.

Cities have, because of 20 years of community development block grants, and now 4 years of HOME, cities, by and large, have pretty good people nfrastructured towards producing housing and operating housing assistance programs, tenant-based assistance and neighborhood redevelopment.

Cities by and large have a good people infrastructure to do that and have a good handle on it. States do not. And there may be some exceptions to that but the States I'm familiar with, the cities are way ahead of the States. And it's logical. It's because a neighborhood is in a particular city and the local officials have to deal with that neighborhood every day. And the State is somewhere off in the State capital.

So the resources and human resources tend to be at the cities, rather than the States.

Senator MACK. OK, I think that, frankly, that covers most of the questions that I have.

Mayor BARTLETT. If you don't mind, I have one other that I failed to mention. I realize I really need to.

That is FHA. There is a sort of a theoretical debate that occurs among conservatives particularly as to whether the purpose of FHA, and I spoke about the need to privatize FHA and make it a Government-chartered corporation, as opposed to a Government-owned corporation.

Within that context, though, FHA is a very powerful agency for home ownership opportunities in this country.

In the 1950's and 1960's, FHA was given, loosely speaking, the mandate of ensuring single family homes for that class of people we called the returning war vets, and as they built families, and it did that very well.

Unfortunately, the easiest place to do that is in the suburbs. And so FHA became in fact a force for those new tract houses, subdivisions for that went to the suburbs, a positive force for that, but neglected the inner-city.

For years, up until recently, FHA was the source of the redline maps in the Nation's cities. The Congress, in chartering FHA, should consider the power of FHA mortgage insurance and use that power to give FHA the new mandate of central city redevelopment, inner-city redevelopment, ensuring mortgages back into the central city, particularly for first-time homebuyers but with that as its mandate.

FHA then could, not by doing the same things that they've done for 40 years, but by doing new kinds of insurance activities, could be an enormously powerful force or central city redevelopment and specifically for home ownership opportunities in the central city.

But Congress has to change the mandate or the charter. So whether it's—and I've advocated a Government-chartered corporation. But whether it's a Government-chartered corporation or any other kind of structure, change the mandate.

FHA has been multifamily for the central city, and single family tract houses for the suburbs. We need to eliminate the multifamily. That's working just fine. There are multifamily opportunities throughout America and hroughout central cities.

Eliminate that. That can work without the benefit of FHA insurance. And then convert the power of mortgage insurance FHA, convert that power into a central city focus so that you can ensure home ownership opportunities for residents of central cities.

That one change would do more for neighborhood redevelopment or for central city redevelopment, or for home ownership than all of the others combined.

Senator MACK. How far would you go with that, Steve, in the sense of what you're really talking about is refocusing FHA's attention and direction and finances into the redevelopment of urban communities. How far would you go?

I mean, would you in essence just move their mandate from suburbs to?

Mayor BARTLETT. I would move their mandates from suburbs to central cities.

Senator MACK. Are you in essence saying no longer provide——

Mayor BARTLETT. You can't get past the homebuilders on that one, so I wouldn't even try.

No. But the beauty of FHA and Fannie Mae is since it doesn't really access Government money, there's not a finite limit on the amount of money available. It's all recirculated through the secondary mortgage market.

So you don't have to take away from the suburbs in order to focus on the central city. If you focus on the central city, tell them that that's what their charter is, that's what they have to report to Congress on, give you real numbers, develop parity, and they will do it. There are techniques that can be done.

I'll give you one example. I'm not an expert at FHA but one example, the barrier in the central city towards new home construction, single family construction, is a barrier of infrastructure, blocking up enough lots in one place so that you can have five houses in a place instead, so in essence, the central city equivalent to a subdivision. The barrier is sometimes streets and sidewalks and water and sewer lines, just as it is in the suburbs, except you have to redevelop it.

So put FHA on the mission of ensuring those blocked up, they don't have to go out and use eminent domain and buy it themselves, but just provide the insurance to a private homebuilder that goes and blocks up five houses or ten lots in one place and provides that insurance.

A homebuilder can't do that if he can't get mortgage insurance for that small little central city subdivision. He can get mortgage insurance on a vacant piece of property of a 150 acres in the suburbs. So it's a matter of leveling the playing field.

Senator MACK. Just one more question that comes to my mind, as you mentioned home ownership.

What more do you think that HUD can be doing with respect to home ownership?

Mayor BARTLETT. Make every program that HUD has with a home ownership component. I mean, it's as simple as that.

I read the Blueprint's words on page 3, which were very nice. I mean, it goes on for the entire page actually about the benefits of home ownership. But there's not a single programmatic change.

Here's one. FHA is one, as we discussed.

The second one would be to take the Section 8 vouchers, of which there'll be more as a result of this, the tenant based assistance, and allow someone to use that voucher to pay their mortgage or to pay their rent at their choice.

You see, that's not really complicated. If you decided that home ownership opportunity is our number one goal for all income levels, and if we've decided to pay the housing costs of x number of low-income families in America, then why shouldn't we be willing to pay their housing costs by helping to pay their mortgage instead of helping to pay their rent?

But all of the Federal law for low-income families is biased for rent tenant-based and against home ownership. So convert FHA

and then just take the existing programs and make all of them eligible for home ownership.

Senator MACK. Senator Kerry.

OPENING COMMENTS OF SENATOR KERRY

Senator KERRY. Thank you very much, Mr. Chairman.

Mr. Mayor, welcome. I apologize for not being able to be here for your testimony.

But let me just ask you, if I can, quickly. I gather that you proposed the notion or you've endorsed the concept of the full voucher, just open it up and let the vouchers go.

A lot of folks are concerned. I mean, these are issues that have arisen before, but you're going to wind up with problems on the access, as well as just the market response.

How would Dallas particularly be affected, do you think? And is Dallas different from New York or Boston?

Mayor BARTLETT. Well, every place is different than New York, but of other large cities.

Dallas and every large city that I know of would benefit from such a full access because in fact residents, if you empower residents with the ability to choose their own housing and pay their own rent, they will find that housing. You have to eliminate the current—or you don't have to, but in order to make it work, you have to eliminate many of the current regulations that exclude large segments of housing from Section 8.

But if you eliminate those regulations, then in fact residents do and can find their own housing.

In Dallas, for example, we have 7,500 Section 8, tenant-based Section 8 certificates. It is an invisible program that is well-liked, that is well-administered. Ninety-six percent utility, so it's only the turnover.

People live in desegregated conditions, places where they want to. A public housing program, and we have a well-run public housing agency now, we didn't 5 years ago but we do now by all certifications, and yet the controversy and the difficulties of living in public housing are rather well-known. And public housing residents would tell you that they would rather get into Section 8, so they walk with their feet, but there are barriers to doing so.

Senator KERRY. Well, except that aren't there limitations in our ability to continue to make more Section 8 available?

Mayor BARTLETT. Same limitations as your ability to make public housing available. Same limitations.

Senator KERRY. Not really. Isn't it far more expensive?

Mayor BARTLETT. No. In fact, if you take the total cost of public housing versus Section 8, the total cost is much lower using tenant-based certificates. There's actually, I got that, there's a chart in the January version of the Blueprint. The total cost is far less expensive.

Senator KERRY. But that's, what's the relative unit numbers and what are the relative levels of income. I mean, that affects total cost?

What's the population comparison between the two, current Section 8 and——

Mayor BARTLETT. It's the same people. Section 8, you pay 30 percent of your income as rent, and in public housing you pay 30 percent of your income as rent.

Senator KERRY. No, but I mean in terms of fixed numbers of people who are currently in the numbers of units. I should know; I don't know.

[Pause.]

Mayor BARTLETT. Let me, I didn't mention this, I had it in my written testimony, there's a regulation, for example, that you could help—people who live in public housing try their best to move into Section 8. There is a section of Federal law that prohibits them, for example, which is odd, but it does, and that is you go on a waiting list for Section 8, and if you are on a waiting list for tenant-based Section 8, and if you live in public housing, you cannot get to the top of the waiting list.

I mean, it's the craziest thing you've ever seen.

Senator KERRY. Well, let's assume they walk with their feet? Do you see a lot of seniors and people with disabilities walking with their feet?

Mayor BARTLETT. When they're given an opportunity they do. Now many of those, both seniors and disabled, as well as others, who live in public housing units that are decent and modernized and good places to live, they would stay right there because it would be a good place to live in this home, and they like it.

But if they want to leave, if you give them the right to leave, they will if they want to, and the test is whether it's better housing or not.

Senator KERRY. What happens if the rental base in a particular community then starts to inch up and the vouchers don't?

Mayor BARTLETT. That happened in Dallas actually. Dallas officials came to HUD and showed them the new rent schedules and HUD adjusted the rent schedules. That's the way Federal law is set up, to adjust the rent schedules to move up.

Senator KERRY. Does that then become an unfunded mandate and an entitlement of its own kind where private sector just raises the rents and HUD's forced to meet that?

Mayor BARTLETT. No, because the rents are based on the market.

Senator KERRY. How do you prevent that from happening? The market decides the market's higher?

Mayor BARTLETT. The market is based on supply and demand and so if you, the Federal tenant-based certificates are not going to dominate the market. The market will be based on marketplace economics, and the Section 8 certificates is just simply one way of paying rent.

So the way you prevent it is you allow people to lie where they want to, and then they go into the marketplace and they find market rate rents and use the voucher to pay. It works very well. I mean, I'm telling you success.

Now if HUD gets in the way, as sometimes it can, and imposes artificial ceilings on what they call market rate rent, well then that can have the effect of driving Section 8 certificate holders into segregated, less-than-standard housing, no different from public housing, by the way, not quite as bad, but it does have that effect.

But if you let the marketplace determine the market rent, then it doesn't have that effect at all.

Senator KERRY. You don't think that this might make housing programs in America actually far more expensive rather than less?

Mayor BARTLETT. The evidence is quite the reverse. The private sector, in terms of production, builds houses, whether it's single family or multifamily, less expensively and operates them more beneficially than the public sector. That's why people want to live in private housing instead of in public housing when they're given choices.

Senator KERRY. Well, that's interesting. I mean I wish that were always true. It isn't always true. There are a whole lot of slumlords around in the private sector who never bring an apartment up to code, who don't spend the money, the heat's turned off, the faucets don't work, the places are infested with rodents, and they don't spend a penny to make it more livable, and they are still in the private sector.

Now if you suddenly suggest that people can walk with their feet, and there's a voucher, and off they go, leaving an equally decrepit public housing distressed property, and they go out into the marketplace, suddenly the private sector says, aha, we've got this new source of revenue. The Government is supporting, you know, us, rather than off in this sort of competing entity, and so the rents start to rise. But where's the guarantee that the service quality of the particular house is going to rise with it?

Mayor BARTLETT. If low-income families or middle-income families, just like middle-income families or upper-income families, if they are given a choice to live where they want to, and for some number of them, the Federal Government will pay their rent through a certificate, they will choose those places to live that best suit their needs.

If someone's given a choice, they will choose a place where the faucet works. Now, much of our current structure, they're not given a choice. They're told they have to live in a place where the faucet doesn't work. But if they're given a choice, they will choose a place where the faucet works.

So the classic slum landlord will not be able to access, will not be able to access Section 8 certificate holders because those certificate holders can pay rent in decent places to live, and so they'll move.

That actually does happen, Senator.

Senator KERRY. It does happen in some cases. I don't disagree with you. But the other thing also happens in some. I mean, not everybody is as competitive in the marketplace and they all play the market in different ways.

My concern is also—I mean, I'm not adverse to it. I'm just trying to think it through carefully and see what the unintended consequences become.

What happens to the housing that is then vacated when they walk that's owned by the public?

Mayor BARTLETT. Well, first of all, let me say that, in my opinion, most of the current public housing in America and in Dallas, if privatized, would continue to be operated in full for low-income

residents who have chosen to live there because they are decent places to live.

So most, not all, but most will continue to operate under either a public housing authority, or non-profit, or the city, or a private for-profit landlord, and will continue to operate as housing.

It will be better housing because it will be more competitive.

The ones that will be dilapidated will be removed, will be those locations which, either because of location or because of age, or because of being so dilapidated that the repairs don't justify, it can't work out in the rent, they will be removed.

The people who used to live there will be living in better places, closer to better schools in better neighborhoods, closer to jobs, and with faucets that work.

So by putting marketplace economics into public housing, you benefit everyone, but because the tenants that used to live in public housing won't live there anymore, and that public housing wasn't worth living in, so it will go away.

But you're helping the same number of people.

Senator KERRY. Where would you put your enforcement mechanism for situations where a family of color or some particular ethnicity or religion shows up with a voucher and their voucher's as good as anybody else, but they are refused entry in one guise or another?

Mayor BARTLETT. Well, if it were my choice, I would convert that over to the Department of Justice. I think HUD is the wrong place to try to enforce civil rights laws.

It is the Open Housing Act of 1968. It is enforced vigorously in every city that I know about. Every city has their own ordinances and it is enforced vigorously.

So that was an issue in the 1960's and the 1950's, and to some extent in the 1970's. But in the real world, open housing exists today.

Now there is one element in which open housing is prohibited by the unintended consequences of one particular Federal regulation, which ought to be abolished. It was abolished, by the way, in last year's housing bill that Chairman Mack and others were involved with, Senator Bond and others, but it died in conference committee.

That is there is a provision of Federal regulations that says that if a landlord takes one Section 8 certificate, the landlord has to take all Section 8 certificates. And so many landlords, if they are already full or close to full, if they have a location that they can keep it full without Section 8 certificates, they choose not to take any because they don't want to take all.

The result is that some of the better multifamily units are denied to Section 8 resident certificate holders by Federal regulation. Repeal that Federal regulation and you would dramatically open up the access.

But that's not the landlord's doing; that's the Federal regulation.

Senator KERRY. Thank you, Mayor.

Thank you, Mr. Chairman.

Senator MACK. Thank you.

Again, thank you, Steve.

The second panel is Richard C. Gentry, Mr. Audley Evans, and Reverend Willie F. Carter.

[Pause.]

Senator MACK. Mr. Gentry, why don't we go ahead and start with you.

Again, I welcome all of you.

If I can, I just on a personal note, while I had the opportunity to say hello to all three of you when I came in, Audley Evans and I go back several years and I might say in his education of me with respect to public housing issues. And the work that he has done, there is a tendency, when we get into these discussions to talk about buildings, bricks, mortar, finance, dollars, and all of that, and don't spend very much time talking about the people who live in public housing communities around America.

One of the things that Audley was able to do was really to open my eyes and help me understand the concerns and the problems that are facing the people who live in public housing.

And so I'm deeply indebted to him for that experience and that knowledge, and so I especially welcome you.

Mr. Gentry, if you would go ahead.

STATEMENT OF RICHARD C. GENTRY, EXECUTIVE DIRECTOR, RICHMOND REDEVELOPMENT AND HOUSING AUTHORITY, VA

Mr. GENTRY. Good morning, Senator Mack.

My name is Rick Gentry. I'm the executive director of the Richmond Virginia Redevelopment and Housing Authority, and I very much appreciate the opportunity to be here this morning.

I also have some Florida roots, as well. I have a graduate degree from Florida State and lived in Miami at one time, in addition to Tallahassee. I really appreciate your allowing me to be here.

Also, for purposes of my testimony, in addition to my record as the director in Richmond, where I've been for about 5 years, I was previously the executive director of the Housing Authority in Austin, TX, which was troubled at the time that I took it over, which we were fortunate enough to turn around while I was there.

I was also involved, before that, as the director of operations with the Housing Authority in Greensboro, NC, as well as an employee with the Greensboro HUD Office back in the 1970's.

I'm also currently serving as senior vice president of the National Association of Housing and Redvelopment Officials, which is a 9,000 member professional association that's been in existence for over 60 years.

And my testimony this morning will reflect not only my own views, but also the considerable dialogue and networking with fellow professionals throughout the country.

Senator MACK. Very good.

Mr. GENTRY. Also, I have an extensive statement prepared and submitted to you. I'm not going to try to reread all of that, but just hit a couple of points, and I would be glad to respond to any questions you might have during the process.

I believe that Secretary Cisneros and the Department of Housing and Urban Development should be applauded for the most positive benefits of the HUD Blueprint, which was to completely open up the debate concerning the future of our programs.

Rather than approaching program improvement from the basis of tinkering with current programs, the Blueprint proposes major re-

form and has set the stage for many of the proposals which are before you during this period of your deliberation.

Unfortunately, the HUD proposals for the public housing program, which is slated for the most major change, are deeply flawed.

They are flawed in that these proposals continue to call for a uniform, mandated, cookie-cutter approach for the programs that deal with the issues of some 3,400 public housing authorities throughout the Nation.

Many of the problems we face today are the result of a program which is built on the HUD-mandated notion that one size fits all.

Market conditions, housing stock, housing needs, program size and profile vary across the country among the various local programs. And the conversion wholesale of public housing to vouchers would work in some localities but it is not workable in others.

In any event, the notion that a program flawed by the disfunction of a centralized top-down design that can be cured by the imposition of another centralized top-down design is just simply wrong.

There is an argument that basically the flaw is in 2 parts.

No. 1, is as to cost. There is the notion that has been expressed that somehow voucherizing public housing would lower the cost to the taxpayers.

That is simply not true.

There are some figures that I would refer you to that would have, I think, particular relevance to you. Back in November, the Staff of the Senate Appropriations Committee on Housing produced a paper, Stephen Kohashi in particular, that among other things, dealt with the relative cost of vouchers versus traditional public housing, and it showed a dramatic difference.

What Mr. Kohaski's paper showed is that, in comparing the current cost of Section 8, which is our voucher program, versus the current cost of public housing, the difference was about $2,000 per family per year more for Section 8 versus public housing.

This has taken into account the cost of operating subsidies and modernization in public housing versus the cost of vouchers entirely.

If you add back in the cost of debt service and development of new public housing, then it makes the figures more equivalent, so that you can make a case either way.

But for existing housing, where the cost of debt service of building the properties has already been taken care of, the cost of Section 8 is dramatically higher.

What that means is that for the same Federal dollars, you serve fewer families. If you serve the same number of families, then there's a need for a greater amount of taxpayer money to fund the programs.

In the current climate, I doubt seriously that we're going to see more money flowing into public housing from Washington than we have in the past.

In saying that, I don't want to mislead you. Section 8 is a wonderful program. In Richmond, VA, I currently operate about 4,500 units of low-income public housing serving about 13,500 individuals.

We also operate about 2,500 units under the Section 8 program which serves an additional 5,000 individuals. Both programs work, both programs are fine.

But the issue is not so much whether one size fits all, as opposed to the local community being able to make its own decisions for its own programs.

What I'm afraid will happen if voucherization were forced on all public housing properties, regardless of local conditions, is we would not see a wholesale exodus of residents from public housing, but what would happen is we would lose a significant minority of our residents and therefore lose our financial margin.

The 4,500 families who live in my public housing would not all move out into the private sector; there simply aren't the houses there to accommodate them.

But I would lose, I dare say, 10 to 20 to 30 percent of my residents, who would take the subsidy with them, and who then I would have to replace from the market at market rents.

Now my units of public housing in Richmond are good units. I consistently have a vacancy rate of less than 1 percent with ½ of 1 percent, last month, and reflects only turnover.

Every one of my units meets city code, but it's public housing. It was built back in the 1950's and 1960's, primarily, when public housing was designed under different standards.

If we lose our margin of operation, and public housing has a very tight financial margin, then we lose the ability to serve the remaining families.

What I would submit to you, and what the NAHRO proposals detail, which is attached to my statements, is a form of direct grants to local agencies where the local housing authority is standard or high performing.

The local housing authority would be required to develop a local plan through a local notice and comment process which would take into account the views, wishes, and needs of residents, as well as city officials, the Housing Authority Board and other interested parties. We would develop our own process.

If we choose to voucherize some, part, or all of our stock, and we can show that it would work, we can do so.

If we develop another mechanism, we can do that as well.

I believe that the true choice for the residents is a choice that results in upper mobility. You do that not only by providing sound stock, but also by developing a sane and sensible rent system, rather than the rent system we have now, which actually punishes families for positive productive working behavior.

If we can combine a change in rent structure and rent reform with an ability, with a structuring of programs so that there's a true continuum of options, then you provide for meaningful choice for residents on the local level, rather than an empty choice.

And I'd be glad to respond to questions, Senator.

Senator MACK. Thank you, Mr. Gentry.

Audley.

STATEMENT OF AUDLEY EVANS, EXECUTIVE DIRECTOR, TAMPA HOUSING AUTHORITY, FL

Mr. EVANS. Good morning, Mr. Chairman, Senator Kerry, and Members of the Senate Subcommittee on Housing Opportunity and Community Development.

I'm honored to have the opportunity to speak to you this morning as the director of the Tampa Housing Authority, one which was troubled back some years ago, and most recently I helped in the New Orleans Housing Authority, one which is very troubled now.

I have a very clear and precise firsthand experience as to what running a large housing authority is like, and having changed one to a high performer, which is Tampa, at this time I think I have some knowledge as to how I can view the changes that are taking place in HUD.

I've submitted to you a typed statement but I'm not going to just read it through, but walk through pieces of it that are important, that I think are important.

I think public housing as it exists presently denies residents the rights to choose where to live. Federal law have concentrated the very poor in public housing areas.

Local officials have cited public housing developments as high poverty areas, and have continued to perpetuate that problem.

Federal law also penalizes residents who seek to work presently and keep the concentration in the same place, making it a worse situation than ever before, compared to what exists in any other area.

One thing that's lacking also is that the discipline of the real estate market and industry is not in public housing. Public housing presently has moved to an area of being a social service agency rather than a real estate management agency providing for low- and moderate-income families in the country.

In light of the many problems that have faced the public housing industry over the past 50 years, the proposed HUD Blueprint, I think for the first time, offers some concrete solutions to some of the critical issues that we've faced over the years.

Because of that, in general, I support the HUD Blueprint. It has elements that can be used to solve some of the problems, and it has pieces that need to be changed or improved.

The plan proposes to give direct benefit to residents rather than to the agency or the governmental unit. I support that because for the first time residents will have a chance to choose where they live and it will force housing authorities to maintain units that compete and compare with the surrounding marketplace.

The subsidy process that we have lived through for all these years of public housing allows some, not all, but quite a few housing authorities to become complacent because there's no real reason to bring the units up to the standards to compete with the surrounding neighborhoods because people are forced to come to you, they have to stay with you, so you didn't need to bring them to the conditions to compete.

I think the process of giving the residents a choice will force the housing authorities across the country to go back to keeping their units competitive.

The process of change that HUD has submitted to you, which is that over a transition period of 3 or 5 or 6 years, you'll have to come up to market grade, and you'll have a tenant-based subsidy, I think is good. It needs to be tightened up a little bit. We all know all documents need review over several periods of time.

But the HUD document at least defines some period for transition.

What I would support in that process also, and it is very critical, is that during that transition period, housing authorities continue to receive full modernization subsidy, so they can become competitive.

We also would support the fact that they need to continue to receive full operating subsidy during that transition period so they can continue to improve the housing stock that they have.

I would also urge that HUD is forced to give swift approval for creative alternatives to the current finance mechanism for public housing. That is, if a housing authority can find creative financing to get their units to standard, go ahead and approve the plans and not sit on the plans until the funding or the funding mechanism is no longer available as currently exists in the HUD system.

I think the rent rules should change also, to give more flexibility based on a local market-driven rent base. That is, using fair market rent in the locality to determine what the rent base should be, and the subsidy base in relation to that fair market rent.

The notion of transferring the properties to the housing authorities also that HUD suggested is great, and after that transfer has been made, housing authorities should be supported and given the opportunity to use creative financing to maintain the stock and improve the stock, and also to compete in the marketplace.

In the transition process that has been proposed, though, I think one thing needs to be brought into focus, and it is one that we have somehow almost made perfect in our city, and that is the notion of getting residents involved in the process.

We have started a program in Tampa called REAP, Resident Enterprise Assistance Program. It has now become nationally known in some circles. What in fact does is take residents in an incubator type setting and teaches them to develop small businesses to support the housing industry in which they live, work, and also the surrounding community. We have established over 40 businesses. As a matter of fact, we have graduated over 100 businesses. We currently have contracts with over 40, and we're undertaking a $12 million project right now using resident contracts in joint ventures, so it turns the same dollars in the community, so it changes the whole face—of the entire community.

I suppose I would support and market, that type of development in the process as we change from one of the HUD system to the other, getting the residents involved in the process.

The Davis-Bacon Act also hampers the hiring of residents because most residents are not yet professionals. When you try to hire them with the wage restrictions, it tends to discourage directors from hiring residents in that process.

When you look at the whole notion of management and supervision, I think HUD needs to move back to being a regulatory body, set the rules, review policies that are set locally, and review those

policies on an objective basis, rather than get involved in programmatic activities on a daily basis.

The funding itself should be directed to housing authorities, and also with some relationship to the cities. Visit the cooperative agreements the cities have with housing authorities and also the CHAS. Use those as guiding pieces.

Don't get the State involved. The State basically will just bring another level of bureaucracy to the running of public housing and the delivery of service.

I believe that the changes on hand presently can change public housing as we know it. It will force housing authorities to become competitive. It will force housing authorities to bring their stock up to good quality, and it will take housing authorities out of the mode of being good plantations.

A lot of directors, and there are some great directors, I have good colleagues also in the business, but a lot of directors do not support the notion of tenant-based subsidy because it removes their power base. I know a lot of them supports the current method of subsidy because it gives them that nesting egg that they can sit there and just keep it warm from day to day.

So I suggest that this process would be a good one.

Thank you for giving me this opportunity to talk to you this morning.

Senator MACK. Thank you.

Reverend Carter.

Reverend CARTER. Good morning. My name is Reverend Willie F. Carter.

Senator KERRY. Mr. Chairman, could I ask your indulgence and Mr. Carter's for a moment?

Unfortunately, I have to go down to the White House for a meeting at 11:00 o'clock, and I apologize. But could I ask a couple of questions before I do? And if you want to chime in as part of the answer, I'd appreciate it.

I'd just like to hear, Mr. Evans, your response to the concerns raised by Mr. Gentry and others.

What do you say to the notion that the voucher process would undermine the financial base of whatever remains within the existing public authority?

Mr. EVANS. My answer to that basically is that this entire notion of a free economy leaves one with a basis for you to become competitive. If you're going to give the housing authority over the transitional period the tools to work with, which is continued full subsidy and modernization, that means in a period of time set, you can bring your units up to code using Federal dollars.

Thereafter, you should develop, based on your rent base, a system of management that allows you to remain competitive. And if you cannot do that, you should not be in business.

If we're going to support the notion of saying, well, if freedom is there, for residents to choose, then you're taking away our edge, then we're not in business, we're in a socialized, I don't know what the right term is.

Senator KERRY. Let me interrupt you there to ask Mr. Gentry, and if you want, Mr. Carter, quickly to intercede.

Why shouldn't we wean ourselves from these public enclaves and begin to make them competitive and create a structure where people have greater choice and freedom to move away?

What, I mean, aren't there enough people on a waiting list or people at a low-income level who, if there is a competitive structure within the market, they're going to find there way to one good one or another?

If they don't, then shouldn't the bad be defunct?

Mr. GENTRY. I think, Senator, that there is a dividing principle that reads something like this. That is that no matter how bad things may seem to be, they can always be made worse.

I think that what we're talking about here is using methodology to address all properties and all operators in order to deal with the problems of a few.

There are a number of high profile problem projects in this country, and there are a number of high profile problem agencies that should be dealt with in a different way.

But in most cities where the housing authority is a good operator and by HUD's own standards that were mandated by the Senate some 4 years ago, 97 percent of us are either standard or high performing housing authorities that have good programs.

What would happen, as I indicated while ago, in my opinion, is I wouldn't lose my entire tenancy because the stock is simply not there. Nationwide, something like 40 percent of public housing, not just in elderly highrises but ordinary public housing, is occupied by either the elderly or the disabled, who would stand a lesser chance of moving out.

We have families for whom we feel a need who could move up and move out.

Senator KERRY. If they don't move out, they'll use their voucher to support that existing housing stock?

Mr. GENTRY. Yes, they will.

Senator KERRY. Why not then, why won't the other available spaces fill up?

Mr. GENTRY. They would fill up but probably not at market rents. I could fill them up at the rents that I'm charging now, which are subsidized, but to look for market-based families to move into public housing in most places in the country I think is unrealistic.

I think that the value of public housing is that it fills a spot on the continuum of housing options.

Let me give you an example of how we use public housing to help people move up in Richmond, VA. We have a variety of home ownership options for the families in public housing that choose to work despite a system that punishes them for working.

I would like to address that later, as well, if I could.

Right now, we have privatized a number of our units of public housing in Richmond where we have moved people from public housing into home ownership units, which are not the worst of our units but the best, either single-family houses or semi-detached row houses, where the families have executed lease purchase options.

We also have a relationship with a number of non-profits locally, including Habitat for Humanity, where we send people out of public housing and into home ownership.

And my agency is also a redevelopment agency as well as a housing authority, where we do much urban renewal type programs, typically done by cities directly in many States. And we're able to move people up and out of public housing and into home ownership opportunities.

I think that the choice available to public housing tenants should be more than just a choice of a roof over their heads. It should be a choice that allows a family to improve themselves economically and move into the mainstream of life in this country. And I think public housing can do that.

But if we lose our financial edge by losing a margin of our people, then we would have significant problems serving the remaining families.

Senator KERRY. I thought the theory was going to be that the voucher was going to represent the subsidy plus in order to meet the market rate. So in effect, if that same voucher, it would be worth the same in either place.

No?

Mr. GENTRY. Vouchers are more expensive to the Treasury than public housing is, once the debt service in public housing's taken into account. You give me that kind of money, I can do some amazing rehab in Richmond that I think would make us truly competitive, but I don't think that's going to happen.

According to the Senate's own figures this past winter, once debt service is taken into account, looking at existing public housing, in order to serve families, you're going to have to spend more money, either that or provide a value of a voucher that's so low that it's not going to really be choice.

Senator KERRY. I appreciate that. That's the heart of the dilemma, and I would like to be able to stay here for further inquiry with respect to it and I hope the record can stay open for some questions.

Thank you.

I apologize.

Thank you, Reverend Carter, for leaving it open.

Reverend CARTER. You're welcome.

Senator MACK. Reverend Carter, go ahead.

STATEMENT OF REVEREND WILLIE F. CARTER, EXECUTIVE DIRECTOR, HUNTER'S VIEW RESIDENT MANAGEMENT CORPORATION, SAN FRANCISCO, CA

Reverend CARTER. Once again, my name is Reverend Willie F. Carter. And I'm from San Francisco, where I serve as the executive director of the Resident Management Corporation for Hunter's View, a development under the San Francisco Housing Authority's jurisdiction.

I'd like to also say to my colleagues, I certainly welcome this opportunity to be on a panel with them. I certainly applaud all of the work that they've done for residents across this Nation.

Certainly Mr. Evans, his reputation is known throughout San Francisco and I think just about every other public housing development in the Nation today.

I'm here today to just speak from the residents' perspective. I've heard quite a bit. I've submitted my written testimony and I'm not going to try to reread that verbatim, but I wanted to say that from the residents'perspective, it seems to be the perception that residents, if given a voucher, would just take that voucher and go out into the public sector, but that's not the case.

Residents are fearful across this Nation of whether the voucher system is going to produce. First of all because sitting where we sit today in public housing, we see the conditions that other landlords are presenting to their residents and it's not much more favorable from where we sit to go out into the public sector.

Also the voucher system, I believe, is going to open up an avenue where the private sector's rents are going to skyrocket across the Nation, regardless of what's been said.

If the private sector is going to see this system come into effect, the rents will go up, the moneys that are going to be targeted for low-income people will not reach the targeted population. It will go to the landlords who have now found that there is a new system.

Back to my testimony, I believe today that both parties agree that public housing, as it currently operates, will operate in a functional capacity. And if it's going to survive, it needs to have drastic changes.

The Blueprint that has been submitted by Secretary Cisneros I believe do touch on a lot of the areas that need to be refocused, yet there are areas in the Blueprint that I believe need to be strengthened, such as the resident management corporations. There should be more legislation that gives resident management corporations more authority to manage the properties where they live.

Also, without home ownership incentives in this package, then no resident management corporation or any non-profit will be able to survive in this environment, in this arena.

Public housing resident management and funding control in housing ownership opportunity is the key to transforming public housing developments into viable communities.

Resident management provides employment and entrepreneurial opportunities to a population largely excluded by the private sector. Private developers, private corporations do not hire public housing residents across this Nation.

Once you go in and apply for employment, and you put your address down, you're automatically given—and I served 18 years in the military and after getting out of the military, it took me 18 months to find employment.

I'm a graduate from Fort Valley State College in Georgia and it took me 18 months to find employment. And I had to do that through a union because of the address, not because of my abilities or anything else. Residents just don't get the opportunity to get the employment.

With the reform in any facet, without first looking at the job conditions and making available, letting residents be able to create jobs themselves is not going to work. Residents have the ability,

they have the creative minds to sit back and create work if you will allow them.

I think in my testimony, I pointed out evidence at Hunter's View, the Resident Management Corporation, we now employ 52 residents who were once AFDC recipients, drug pushers, drug users, who are not productive, hard-working individuals in their own community.

We did that by taking Federal dollars that were targeted to the housing authority and we used it at the development to create landscape companies that can now go out and bid on contracts other places and to hire 20 young men who work as landscapers who learn on the job training by first taking development at Hunter's View and landscaping their own community and turning it into one of the most beautiful developments in the city where just about every resident in San Francisco today would prefer to live because of the changes that were brought about by resident management, not because of the authority or any other city agencies, but because residents took control.

We have a resident security operation that pays residents to watch the vacant units once they are vacant that has brought about a security element in the development where, at Hunter's View, once one of the worst drug-ridden communities in San Francisco, today there's absolutely no visible signs of drug use in our community.

There's no drug trade, no drug dealers standing on the corners. What you will find is young men, young women who will get up out of their beds and go to work on a daily basis.

You have children who had never witnessed anyone getting up and going to work, now seeing their mothers and their fathers who are no longer receiving a welfare check, but are going to work on a daily basis.

I believe today if this reinvention package is going to be successful, we have to rethink some of the future policies.

Home ownership opportunities must be preserved and enhanced.

One hundred and thirty-three privatization conversions across the Nation have been placed at risk by the rescission bill currently before the U.S. Senate.

Ceiling rents must be instituted in all housing authorities.

The current system of rent collection, based on the 30 percent combined household income, is the disincentive for employment. Residents will not go to work if they know they've got to pay 30 percent of every income that comes into the home.

If you take 30 percent of the head of the household's income, then if the spouse goes to work, you've got another 30 percent added onto their income, 30 percent on every sibling, offspring that goes to work. Then you're simply not going to get the motivated enough to go to work.

If they're getting AFDC and they know that 30 percent of what they get in AFDC is going to go for rent, then they're going to stay on AFDC. They're not going to go out and work for minimum wages if they don't have to.

So I believe that ceiling rents will provide an opportunity. Resident management opportunities must be broadened to include the

right to compete for the provisions of social services once those services have been block granted down to the states.

Resident management corporations must be exempted from the Davis-Bacon. Davis-Bacon also prohibits, as an employer in the city that has the highest, one of the highest wage determinations of any city that I know of, we can't compete with the wages the unions set. There's absolutely no way that we can continue to pay landscapers, I mean apprentice landscapers at the rate of $14.60 an hour and be competitive. There's absolutely no way we can do this, and we need to have, the new bill must rethink the policy and put policy in that's going to prevent non-profits from having to deal with the Davis-Bacon.

Thank you very much for this opportunity.

Senator MACK. I'm going to build on some of your last comments, and get back to Mr. Gentry, because he's expressed a couple of times his desire to talk about the same points that you've made with respect to rents.

I would just take this opportunity to tell you my own experience, as I've mentioned, being with Audley Evans in Tampa, one of the experiences I had in Jacksonville, I remembered very vividly in a room much smaller than this, with maybe twice the number of people in it, a huge man at the back of the room stood up, pointed his finger at me and said, you know, you guys always tell us you want us to work. And he said, but what you've done is you've put in place everything that discourages us from working.

He said my wife and I went out and both got part time jobs, and at the end of the month we actually had less money in the family, and we were working.

Then he said to me, in essence, what would you do under those circumstances? Lots of people would debate how they would answer that question, but the point is I think most of us agree that when you put in those kind of disincentives, you're going to get exactly the kind of system we've got now.

But with that, I'd love to hear your thoughts that there's more to this thing with respect to rents than just the 30 percent. I don't know particularly when this was put into effect, but in order to be eligible for public housing, don't you have to have less than 50 percent of the median-income in order to be eligible to live in public housing?

Mr. GENTRY. If you'll bear with me, I'll give you a little bit of history.

There are two pieces of legislation that absolutely destroyed the ability of residents to work their way up in public housing. Both of them were very well-meaning. One was done by a bunch of liberals and one by a bunch of conservatives, so I'm going to be bipartisan in my criticism here.

Senator MACK. I might add that there's only one here.

[Laughter.]

Mr. GENTRY. I assume I'm being recorded, though.

There was a piece of legislation passed in 1969 called the Brooke Amendment, named for former Senator Brooke, that stated that no resident should pay more than 25 percent of their income to rent. A motherhood and apple pie statement.

That was coming at the end of a time period where, during the first 30 years or so of public housing's existence, localities established rent systems or rent schedules. And back in those days, there was no operating subsidy. Housing authorities paid for the cost of operations with receipts from tenants. But the capital costs had to be taken care of by the Feds.

The Brooke amendment ended the ability of the housing authority to establish a minimum rent, and it helped a lot of individual tenants but it bankrupted every housing authority in this country.

What had been a sound financial system up to that point was obliterated and housing authorities were forced to go on the Federal dole to get to do the day to day activities. That allowed us to serve poorer and poorer clientele but it destroyed the ability of housing authorities to function independently.

I don't think it's any coincidence that the first list of troubled housing authorities came along in 1979, 10 years later.

In 1981, the second piece of legislation occurred. It was called the Secretary's definition of income for rent, promulgated by former Secretary Pierce, and it was part of the Omnibus Budget Reconciliation Act in the summer of 1981.

What that bill did was to solve the escalating need for a subsidy and blame it basically on the tenants, and said we need to make these tenants pay their fair share. So it raised the percentage of income that the tenants paid for rent from 25 to 30 percent, which was a little bit bad, but then it did something that was horrible, in that it did away with the ability of housing authorities to establish ceiling rents. Henceforth, tenants were to pay 30 percent of their income for rent with no ceiling.

Right now, the dumbest thing I do in my day to day job is the way I charge rent to my tenants. By the time you take into account, Federal income tax, State income tax, the cost of going to work, day care, and 30 percent of gross income to me as rent the protypical welfare mother living in public housing loses money if she goes to work. We've placed her in a position where to be responsible to her family, she's got to be irresponsible to the larger society. To be responsible to the larger society, she's got to be irresponsible to her family. That puts her in a real dilemma.

In that set of circumstances, it's almost an act of moral courage for someone to go to work. It's amazing to me that a full 25 percent of my families in Richmond public housing have employed income, and 12 percent of my families have only earned income, despite a system that actively punishes them.

The reason that came about was not because of any ill will, but it was the oldest law of Washington, DC, which is the law of unintended consequences.

The same law of unintended consequences will come about if the Congress decides to mandate one uniform system to replace the current foolishness we operate under with a new set of mandated rules and regulations.

The answer to me is that the Federal Government should set broad goals, say state broad aims, and ask the questions and require the locality to answer those questions. But the answers to the questions shouldn't necessarily come out of Washington.

If you were to turn the public housing system into a set of local direct grants to the local administering agency, what we would have to do then would be to develop a plan which would be to respond to satisfy the questions you had asked in return for your money, then based on the kind of money you give us, we could define the income level, the mix of people we can serve.

We could define how we would fit public housing into the continuum of housing options in the area, we could develop home ownership connections as we have done I think very successfully in Richmond, VA, and I think that we could make a program fit the needs of a locality, whether it be in Tampa, FL, where voucherization would work there, or whether it would be Richmond, VA, where I would probably choose to voucherize a couple of my properties, but not all of them, and maintain a variety of options.

Senator MACK. Let me hop in here for a second and maybe get the three of you to respond to this. Because one of the areas which you're raising is this idea that some of us have been pursuing, the idea of vouchers, not in all areas. I mean, there's some things that we, I think the issues of the disabled and the elderly may have to be looked at differently, but anyway that's the thrust of where things are going.

But yet we see right in front of us that we have some difference of opinion within public housing as to how fast it should happen, whether it should happen at all, and the argument that says, don't take the voucher idea and impose it on us as one solution.

For example, New York City, I suspect, would have an entirely different attitude than say that Audley Evans is projecting or that Mr. Carter is projecting with respect to San Francisco.

Suppose we said, though, proposed as a solution to try and figure out how one proceeds down this path, is we say to the residents, you decide. You make the determination about whether you want to have vouchers available or whether you want to stay under the old system.

In other words, where I think we ought to be coming from is what is in the best interest of the people who live in public housing. If they live in a good, solid public housing community, which they are apparently very comfortable, as Reverend Carter's been talking about, they're going to react to that and say, I think we want to stay with the present system.

From what I'm hearing Audley Evans saying is that the people in his would probably say let's have a voucher but many of them might stay where they are, and some of them might want to leave.

So what about the idea of saying, as the way to try to solve this problem of the differences of the local communities, whether it's San Francisco or whether it's New York, or whether it's Tampa, or whether it's Richmond, let the people decide.

Since you've had a chance to chat for a few moments, let me get Reverend Carter and Audley to respond.

Mr. EVANS. Senator, I think you've just hit the nail on the head. This system was designed for the people in public housing. We are thrown into the equation as administrators of public housing because it is our business that we are in. But if we go back to the intent of the subsidy that HUD now administers it was intended for the poor people that need it. Why are we in that equation?

Why are we going to assist them to give us the choice and not the people the choice? The people should have that choice, and I think the overwhelming thing, if you talk with the residents, is that they would like to have the choice. Although most of them will stay right there in public housing if it's good stock.

Then what that does, is, it forces the agency to maintain good stock. We talk about losing a part of our resident base. How can you worry about that if you're going to bring your stock up to quality, and why should you be bothered about that as a legislator, because your mandate is to protect the taxpayers' dollars and to protect the people that you're going to serve, which are the residents here.

What we do in the middle as administrators is that we should be forced to deliver, and if we're forced to deliver, we have been given the subsidy to bring the units up to quality, then we should be forced to maintain them where they are competitive, and don't worry about those people who are going to move away because there's a long list of people waiting to move in.

Also, the Senator that was here earlier mentioned the fact that landlords would start jacking prices up. Part of the equation we tend to skip over is the fact that if HUD now transferred these properties that we administer to us with no mortgage, that we have no debt service. So we should be able to deliver these units on the market at a lower rate than any other landlord in our city.

Now if the vouchers, for example, were $300, as an example, I'm just using that number, OK, somewhere along the line, our unit's going to align closer to that $300 than any other landlord who has a debt service to pay on the property that they're going to make available to people for rent.

Therefore, you will find that we will not have vacancies because if the voucher's worth $300 and the landlord is charging five over here, then the residents are still going to gravitate towards you in public housing because they are closer to what you are offering your properties for.

You should not be worrying about vacant units.

What we're forced to do for the first time in this industry's life is to bring a unit up and compete and get off our duff and stop using the subsidy as a crutch to lean on and call for more subsidy every year.

Now for the first time, we can freeze the subsidy in place and make it become market-driven.

Senator MACK. Before Reverend Carter responds, I just want to make a comment though. I agree with what you've said, but there's kind of an underlying tone though that kind of points the finger at some of the failed or failing public housing communities around the country.

I think frankly what Mr. Gentry had to say is that Congress ended up doing lots of things that really affected the ability of public housing authorities around the country to really make it.

We took away their sources of income in essence. And so part of what we ought to be trying to do is to change that equation so that public housing does in fact have the ability to generate that kind of income, and one of those ways obviously is the voucher.

Reverend Carter.

Reverend CARTER. Yes. Senator, I certainly concur with mostly everything that Audley has said here. Basically, if residents were given the choice, they would choose to stay where they are. What they would choose is that the communities and the buildings that they now live in be brought up to the standards of the surrounding elements in their communities.

I don't know if any of you have been to San Francisco to any of the public housing there, but the public housing in San Francisco sets on some of the most, the best property in the city, it's on prime real estate. It overlooks some of the most beautiful views of that city.

Residents would rather have that view than to do anything else. And I'm being honest, I mean, rather than give up the real estate that they now occupy, they would rather stay there and see that property brought up.

Of course, one of the problems in the past has been with the subsidies. The worse that housing authorities perform, the more subsidies they get. They have an incentive to manage poor housing, so when you put a fixture on this subsidy, it forces the housing authorities to bring their properties up to code and up to standards, and the residents would then take their vouchers and stay where they are.

I think the choice should be given to the residents. The voucher system I do believe is a good system.

One thing that I would say is that in the voucher system that where you have non-profits and resident management corporations, that the project base still remain, rather than the tenant base because the residents in resident management corporations, RMC is a publicly elected entity.

The residents of those developments have said, we want to stay here in this development, we want to own this development, we want to purchase this development. And I think that, in those instances, the vouchers should be taken and be able to be used not only toward rents, but they should also be applicable toward the mortgages and toward home ownership.

Senator MACK. Mr. Gentry, do you want to respond to that thought that I had about letting the residents decide whether they should go into a new system or remain in an old?

Mr. GENTRY. I think they should have a predominant say in it, yes.

But I think that the overriding genius of the Housing Act of 1937, which is our basic piece of legislation, and which has survived intact for many years and it's provided a good basis for our programs, that Act recognizes the proper role of a federated system of Government. That the Federal Government should not be involved in the business of dictating the day to day affairs in the localities.

To me, the Federal Government does three things very well. It collects and distributes money very well. It provides broad goals and directions very well. And it provides prohibitions very well.

The civil rights laws that have transformed my part of the country and yours over my life time have been truly outstanding.

But when the Federal Government gets to the point of dictating how things are actively done, it almost uniformly screws up. Be-

cause the same things that are mandated for Tampa, FL, Richmond, VA, San Francisco, New York, Seattle, San Diego, San Antonio, when they're the same, they cannot work in every locality. Therefore, there has to be a devolution of decisionmaking to the locality as Mayor Bartlett said awhile ago.

I think that the residents surely should have a predominant say in what is done, but so should the locality. Because what may well happen is that what happens to a property is of profound importance to the city, the surrounding neighborhood, and the people who have not been mentioned yet at all, and that is the people on the waiting list who need to have a resource available for them as they come into the system, as the people who currently are being served hopefully move out and into the larger society.

Senator MACK. Reverend Carter, I want to go back to some of the comments you made and some of the things that were in your statement, and it has to do with home ownership, which I think is, I mean it has to be a major portion of what we do.

There has been lots of criticism, though, about the program. Mainly critics have claimed that Government is setting residents up for failure because they don't have the resources to become homeowners, nor do they have an interest in buying public housing units.

I assume, from what you said, that you don't agree with that?

Reverend CARTER. Yes, I disagree with that strongly. In San Francisco, you have a high percentage of residents who have occupied the same unit for 37 years, 47 years, and if they were not interested in that property, they certainly would not stay there that long.

I perceive that there's a misconception that residents prefer to be given handouts or be put on subsidies. I think we've all gone over that, that if residents had the opportunity, and there were no penalties applied upon them to go out and get jobs, they would.

Senator MACK. What is your plan, though, for converting your community to home ownership?

Reverend CARTER. Currently, we are working under the 5(h) home ownership plan that was done by HUD, and we're doing it through, for the past year, we've been in dual management with the San Francisco Housing Authority, and which the residents have taken over parts of the everyday maintenance of the development. We've gone into some levels of the property management. And over the next year, we plan to be in total management and do everything that the housing authority does today, while bringing the property up to the applicable codes in order to apply and do the first sales in home ownership. We believe and plan that that should happen over a period of about 5 years.

Senator MACK. That is moving to ownership?

Reverend CARTER. Is moving toward home ownership. We don't think that—everyone at our development has not expressed a desire to buy. We feel that a certain number of those units could be used as the incentive for others to want to buy. Once they see their neighbors buying and see their neighbors taking the responsibilities to take care of the neighborhood, we believe it will start somewhat of a domino effect in the community where everyone will be more interested in instead of receiving a welfare check, or assist-

ance, you see a neighbor going out, buying a new car, you see your neighbor doing things in their yard, it would put the pressure on the next door neighbor to do better.

Senator MACK. I have one more specific question I'd like to ask of Audley Evans, and that is under the Blueprint, it doesn't call for vouchers I guess in phase two or three. In other words, it's some time down the road.

Are you of the opinion that there ought to be some public housing communities that can go to vouchers immediately?

Mr. EVANS. Yes. I think there are some that are ready, and some that have to be phased in, because I think they should be brought up to proper codes over that phase-in period before the vouchers are assigned to them.

Senator MACK. Would your public housing authority be one of those that would be ready to go to vouchers immediately?

Mr. EVANS. I think we are fairly ready. If you compare our housing stock with the surrounding neighborhood, we are in better shape than the surrounding neighborhood for affordable housing in our city. And I think that is true of most well-run housing authorities across this country.

See, we've claimed that the majority of housing authorities are well run. Only a small percentage are badly run, and we're being blamed by the small percentage. If we are that well run, why should we be afraid of competition?

So we are ready to go voucher and see what the market does and we'll go from there.

Senator MACK. I think I would just give you all an opportunity, if there was an additional comment, a point that hasn't been made that you want to raise.

Mr. Gentry.

Mr. GENTRY. I can leave you with one thought. That there is no one solution that's going to fit all problems in all localities. There should be devolution of authority, there should be local grants to local agencies to make their own decisions within broad categories that you establish.

Senator MACK. Very good.

Audley.

Mr. EVANS. One thing I'd like to leave this body with is that in that transition process, microenterprise for residents should be brought to focus. As you transition these units and make them market ready, residents should be involved in that process, should be trained, given the opportunity for training and hiring to bring the units up to code.

I agree with Mr. Gentry that there's no cookie-cutter method to solve the problem and there should be some type of choice. But I think this is the first time we're put in the process where it relates to what the rest of the market drives, which is the resident, the occupant, whatever you want to describe them as, now has a choice where they live as opposed to a system telling them you've got to live here, or you can't move, because if you move, we won't subsidize you because there are no Section 8 vouchers for you.

Thank you.

Senator MACK. Reverend Carter.

Reverend CARTER. Yes. Senator, I would like to just leave with the Committee today that if we are truly interested in providing good housing for the targeted community, the most vulnerable, then we must first remember that in order to build strong communities, we must, in order to get good strong communities, we have to have strong people. Creating strong and productive people is directly related to the existence of strong and productive communities.

Other indicators that this structure's attainable, you can look right here in Washington, DC and just travel over to Kenilworth Parkside and see a community that's thriving because of the resident management there, and in just about any place, like LeClair Courts in Chicago, and take a trip out to San Francisco and see the Hunter's View community.

In order to have a strong community, you've got to have strong people that are willing to do what needs to be done in those communities and it must be done at the community level.

Senator MACK. Well, thank all of you very much. I appreciate your input.

[Pause.]

Our final panel: Shirley Dykshoorn, James Logue, William Frey, and Danette Jones.

[Pause.]

Again, I welcome all four of you this morning, and I look forward to your testimony.

Ms. Dykshoorn, I understand that you have a plane to catch, and so why don't we go right ahead with you, and if you would start with your testimony.

STATEMENT OF SHIRLEY DYKSHOORN, DIRECTOR, OFFICE OF INTERGOVERNMENTAL ASSISTANCE, ND; REPRESENTING THE COUNCIL OF STATE COMMUNITY DEVELOPMENT AGENCIES [COSCDA]

Ms. DYKSHOORN. Good morning, Mr. Chairman.

Again, my name is Shirley Dykshoorn and I'm here today representing the Council of State Community Development Agencies. I am the director of the Office of Intergovernmental Assistance in the State of North Dakota.

I will briefly summarize the written statement that has been provided to you.

COSCDA members are State executive branch agencies which are responsible for a fairly broad array of Federally funded, as well as State funded resources in the areas of housing, community development, and economic development.

As you'd heard this morning, there was some comment about State bureaucracies, and I hope that we could counter some of the perceptions that State governments are not as sensitive perhaps to managing these resources.

But with the very wide range of resources we manage and the breadth of problems in delivery systems with which we work, we believe that COSCDA is in a unique position to make some observations and recommendations on national housing and development policy.

We welcome the opportunity presented by the 104th Congress to fundamentally reexamine national housing and development policy.

As I think a number of us have, I have worked in State government for over 20 years and have seen what works and what doesn't work within these programs.

Although we limit our testimony to topics directly under the jurisdiction of this Subcommittee, COSCDA believes that Congress should review housing and development programs across Federal agency lines in order to develop a streamlined, efficient, and holistic Federal policy on housing and development that has long term effectiveness, because of course the HUD programs that we work with are not the only housing and economic development infrastructure-related programs that we work with.

COSCDA advocates a set of nine principles for transforming national housing and development policy. Given the many, many options available, ones defending the status quo is put aside. We believe these principles provide guidance for evaluating alternative proposals.

These principles, which are described in our written statement, underscore COSCDA's belief that housing and community development resources can and should significantly contribute to promoting the self-sufficiency of families in communities, again, what the previous presenters had emphasized.

Because the nature of family and community problems, the utility of delivery systems and the available resources vary enormously across the country, States and localities need flexibility in using those Federal resources.

This flexibility must include two characteristics. First, Federally funded programs must be deferential to a large degree in the setting of priorities, the use of funds, and the use of delivery systems.

This differential flexibility does not toss aside accountability but focuses accountability on local decisionmaking processes and on subsequent review and assessment of performance.

I guess in talking about this in terms of accountability and local decisionmaking, in some cases you have rural States, such as ours, which have a relatively small population. We don't have Dallas's, we don't have New York City's in our State. But the State government does have a role in looking at how those decisions are made and how dollars could be best used.

Second, Federal programs must not only be adaptable and flexible, they must not be constrained by undue regulation. I know some comments have been made about Davis Bacon and other requirements, and we do have some concerns about the underbrush that the regulations force us to comply with.

Our programs are laden with requirements. To cope, a grantee must become a Houdini to solve these requirements and simultaneously figure out how to meet the program's primary purposes.

Too many resources are spent on meeting those underbrush requirements. It's not too much of an exaggeration to suggest that the major purpose of the program is often lost.

As Congress rewrites national housing and development policy, we respectfully suggest that you consider answering these questions.

What is the fundamental national purpose of the legislation and what are the one or two priority and necessary national goals and objectives?

What are the basic civil rights and citizen protections that should be included?

What are the activities that cannot be undertaken with the funds provided?

How will grantees be held accountable in mutually agreeable terms for their performance?

COSCDA believes that fundamental change must be made in national housing and development policy and that there are many alternatives that are preferable to the status quo.

Before outlining our preferred alternative, I want to stress two priority themes that any alternative we believe should encompass.

First, programs must be simple. Secondary and tertiary objectives must be avoided and nice but not necessary and marginally related requirements cannot complicate our use of resources.

The priority we attach to this theme lends us to support an alternative that essentially starts from a blank slate.

Second, programs must be adaptable and flexible, and must facilitate the tailoring of resources necessary to address circumstances that vary across the country, even within States and over time.

We have reached the point, both with our experiences and the nature of our housing and community development programs where most stand alone projects, picket fence type resources, and myopic visions simply will be unsuccessful, ineffective, and meaningless in the long run.

Although COSCDA has not had the time to spell out in detail a specific proposal that we hold as our priority preference, we are able to outline what we believe is the best approach to the changes necessary in national housing and development policy.

First, we recommend that CDBG, HOME, McKinney, Rural Housing Loan and Grant, and Randall Assistance Programs be consolidated into a single housing and community development fund.

We also recommend that this fund be allocated so that a minimum of 40 percent is allocated to States and the balance to entitlement localities, and that States be able to use these resources statewide.

We already are doing some of that with the HOME program within entitlement jurisdictions, and in fact, in our State, the entitlements chose to work with the State, rather than to get their own money directly.

To a large extent, the families and communities that are eligible and targeted for assistance by one of HUD's current programs or USDA's housing programs are assisted or targeted by nearly all the others.

It makes no sense for HUD and USDA to develop unconnected and usually different and often conflicting guidelines for these singular programs.

It also doesn't make sense for grantees or governments, including the Federal Government, to develop multiple and cost ineffective administrative bureaucracies, applications and grant requirements.

It makes no sense to force intended beneficiaries to jump over hurdles or through hoops to get the kind of assistance they need to improve their lives significantly and for the long term.

It makes no sense for Congress to establish appropriations that cover several related programs and thereby set very similar resource ratios and fund patterns for these programs for all States and entitlement localities when we know that problems and priorities differ.

Second, COSCDA also recommends that States be given the option of having policy management responsibilities for balance of State public housing. We recommend this as an option.

There's no implication that States must or should take on that role but there may be some States that choose to.

COSCDA does believe that several States will initially decide to take on such a role if that role meets the tenets outlined in our written statement.

Over time, we believe that many States would offer such a role.

COSCDA believes that this public housing recommendation will accomplish two very important objectives in the long run.

First it would begin the process of rationalizing and integrating housing and related assistance through much of the State.

Second it permits States to make decisions in relative concert with public housing authorities and others about public housing issues, which is a much better approach.

Senator MACK. If I could get you to wrap up?

Ms. DYKSHOORN. Yes.

In closing, Mr. Chairman, our recommendations for major changes in the national policy shouldn't be interpreted as saying that all Federal housing and development policies are flawed. There are programs that are working well, such as HOME and CDBG, and we think there's much more potential in the McKinney consolidation.

I thank you, Mr. Chairman.

Senator MACK. Mr. Logue.

STATEMENT OF JAMES L. LOGUE III, EXECUTIVE DIRECTOR, MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY, REPRESENTING THE NATIONAL COUNCIL OF STATE HOUSING AGENCIES [NCSHA]

Mr. LOGUE. Mr. Chairman, thank you for the opportunity to testify before you today.

I am here on behalf of the National Council of State Housing Agencies. NCSHA represents the housing agencies of the 50 States, District of Columbia, Puerto Rico, and the U.S. Virgin Islands.

I am Jim Logue. I work for Governor John Engler, as executive director of the Michigan State Housing Development Authority.

Under the former Administration, I served as HUD's Deputy Assistant Secretary for Multifamily Housing under Jack Kemp.

Mr. Chairman, State FHA's recognize that Federal budget constraints and HUD's own limitations——

Senator MACK. Can I get you to pull that microphone just a little closer?

Mr. LOGUE. Sure.

HUD's own limitations require Congress to change the way that Federal Housing Assistance is delivered.

We believe that Congress should rewrite Federal Housing policy to help those who need it, while substantially reducing bureaucracy, eliminating failed housing programs, reducing budget costs, and empowering the States.

The Administration's reinvention plan moves in this direction, but it leaves HUD with more responsibility than it has capacity, and continues to insist on unnecessary and burdensome program regulation.

As you rethink Federal housing policy, we urge you to do the following:

Reduce the Federal housing budget through every practical program efficiency, while maintaining a Federal investment adequate to sustain at least the present level of Federal effort.

Give States maximum flexibility through housing block grants to efficiently and creatively deliver the Federal affordable housing assistance.

And assure affordable home ownership and rental opportunities for lower income and under served families in all markets under all economic conditions by continuing to provide for Federal mortgage insurance.

Federal Housing Assistance should be allocated under block grants within broad guidelines which Congress provides.

In structuring block grants, we urge you to consider the following: State FHA experience, capacity, and proven programs justify restricting housing block grants to States.

At a minimum, States should receive the 40 percent allocation they receive under the HOME program.

You will note this differs somewhat from Mayor Bartlett.

Senator MACK. I did pick that up.

Mr. LOGUE. Not surprisingly.

I do take issue with the comments that States are, in many instances, something that is in the way of Federal Housing programs. I find that just not credible and the facts I think would bear me out.

States do operate, and over the last 15 years have provided the most innovation in housing in affordable housing programs in the country. That's really been the incubator for new and innovative ways of doing housing.

Just to give you an example, in Michigan, of what has happened and what would happen if the State wasn't there.

In Detroit, which is still one of the 10 largest cities in the country, 70 percent of all the new residential housing starts in the city since 1975 have been assisted with housing finance agency, State housing finance agency financing. I would submit to you that without the State's role, that 70 percent of all the housing starts wouldn't have occurred.

Now, that's not to say that the city doesn't run good housing programs, but they just do not have the entire capacity at hand to do the job that is necessary.

We have worked in Michigan very successfully with many cities in combining resources and we think that the resources at the State level have made the difference in many cities for doing that.

Just a couple of other facts.

The States typically run the mortgage revenue bond and the major multifamily tax exempt financing programs in each State.

States uniformly allocate low-income housing tax credit at the State level and do it very effectively and very efficiently.

We, again in Michigan, to give you a specific example, have financed over $3 billion worth of affordable housing throughout the State. $1.5 billion of that has been done completely on the State's credit.

Now I would suggest to you that it is unfathomable to think that $1.5 billion of uninsured housing would have been created in cities, were it not for the State's role in that.

So to suggest that the States shouldn't have a substantial role in any new Federal block grant program I think just flies in the face of the facts.

I would be happy to answer more questions about that but I think you get from where I'm coming.

[Laughter.]

Senator MACK. Actually, all the panelists this morning have been pretty clear about their feelings.

[Laughter.]

Mr. LOGUE. Moving on.

Separate block grant should be established for affordable housing and community and economic development, competition among States and localities to attract new business investment, places a premium on economic development activities that would potentially crowd out affordable housing investment.

The affordable housing block grant should combine all Federal housing programs except public housing and tenant assistance. Tenant assistance funds should be consolidated into separate block grants to States to provide rental subsidies to tenants or to projects.

Public housing programs should be folded into another fund. It should be administered to qualified PHA's who would decide whether to repair, operate, demolish or replace projects, or to provide rental assistance to public housing tenants.

Troubled PHAs' funds should be redirected to States or cities in which they are located. Housing block grant assistance should be limited to home buyers and owners whose incomes do not exceed 80 percent of the area median. Renters' incomes should not exceed 60 percent.

Otherwise, States should have maximum flexibility to use block grant funds as they see fit, including coordinating them with welfare programs.

Funding set-asides or other prescriptive conditions should be rejected, and I would agree that we should reject HUD's performance-based funding proposals.

The continued role in providing mortgage insurance is vital to affordable home ownership and rental housing.

In 1993, two-thirds of all mortgage revenue bond mortgages made in 44 States were FHA-insured. In 20 States, including Michigan, Florida, Connecticut, Texas, and Missouri, over 80 percent of all mortgage revenue bond mortgages were FHA insured last year. That's because of virtually all MRB loans are made for

first time home buyers and most have downpayments of less than 5 percent, characteristics common to FHA insured but not privately insured mortgages.

Likewise, the elimination of Federal multifamily mortgage insurance would severely limit the production of affordable rental housing. Congress recognized this last year when it enacted the multifamily HFA risk-sharing program.

Last year, 28 State FHA's qualified for this new program and nearly all of the authorized 30,000 units have been committed since.

In Florida, for example, nearly 1,000 affordable apartments are being developed through the risk-sharing program that would not be feasible otherwise.

Before I conclude my remarks, I would just like to express the State FHA's concerns regarding Section 8 project-based assistance and HUD's proposal to reduce existing contract rents.

We would like the opportunity to work with you in shaping a reasonable and workable plan in this area.

And I would again thank you for the opportunity to testify.

Senator MACK. Thank you, Mr. Logue.

Mr. Frey.

STATEMENT OF WILLIAM R. FREY, DIRECTOR, NEW YORK CITY OFFICE, THE ENTERPRISE FOUNDATION

Mr. FREY. Thank you Mr. Chairman.

I'm William Frey, the director of the New York City Office of The Enterprise Foundation.

The Enterprise Foundation is a national non-profit organization founded by Jim and Patty Rouse in 1982. We work with community based, non-profit groups to increase their capacity to provide low-income housing and help them build partnerships with State and local governments and the private sector.

Since 1982, we have invested over $1.2 billion in low interest loans, grants, and equity in the activities of more than 500 community-based non-profits in 150 locations throughout the country.

One of those locations is the State of Florida where Enterprise has worked with assisting the beginning of Greater Miami Neighborhoods, and has worked with 36 different organizations around the State. Greater Miami Neighborhoods is an example of an organization which has developed 800 new homes and is in the process and the predevelopment stages of 1500 additional homes.

I'm here to represent The Enterprise Foundation but also to defend New York City.

[Laughter.]

The Enterprise Foundation——

Senator MACK. Why doesn't that surprise me?

[Laughter.]

Mr. FREY. The program in New York City is one of several that Enterprise is involved with around the country. And the base of our program is really working with the community-based organizations located around the city.

This is really where we feel the core of the beginning of a new social partnership has been brought together.

In this effort, Enterprise works with the organizations and in addition to that, we have worked with the Federal funding that has come through HUD in the past, as really the key leverage which gets projects developed in the various sectors.

For example, Enterprise has worked with 55 different community-based organizations around New York City. Those organizations really got an initial commitment of moneys either from the city of New York or from the State, primarily looking at CDBG dollars and more recently looking at HOME dollars as the critical initial component, then bringing in additional investment by the private sector through low-income housing tax credits, getting bank investment to additionally participate in some of the funding of these projects, as well as getting the city or the State to commit its resources.

So it's not just one source but the key source in terms of bringing in the additional funds has been that of the HUD programs.

And this partnership has been instrumental in developing over 5,000 units of housing, all of it for low-income residents. Over 35 percent of it has been for formerly homeless residents.

Another key component to the development of the housing has been Section 8 vouchers. Section 8 vouchers have been targeted for individuals or families who have come out of the shelter system or the formerly homeless system.

It has allowed for the projects not just to be developed as decent and affordable housing, it has also allowed for an enrichment of services to be provided to help get those special needs population back on their feet again and into the mainstream of our society.

So we feel that, again, targeted Section 8 vouchers and project-based Section 8 vouchers are important to the development especially of special needs housing.

CRA is another component which has made a major difference in terms of what has happened in New York City and elsewhere in the country. With the regulations of CRA, it has encouraged banks to become more involved, especially with community-based organizations and the creative financing that has occurred in New York and elsewhere.

Without that, we would not have seen the substantial commitment of the private sector bank financing. And also banks are significantly investing in the low-income housing tax credits in New York City and elsewhere.

Some other points that I wanted to highlight from our testimony that we'd previously submitted:

Enterprise supports HUD's proposal to create the affordable housing fund and the community opportunity fund. The highly successful HOME and CDBG programs should be the foundation for these block grants.

Any consolidation of HUD's programs should be achieved along functional lines. There is clear recognition that one size does not fit all.

HUD's housing function should be kept separate from its economic development function.

Any block grants that are created should have income targeting. We think that this is important, so that CDBG and HOME have

shown the importance of income targeting and ensuring that affordable housing is being developed for very low-income people.

I've addressed the Section 8 issue. We think that it's very important to consider not vouchering out these programs in that we maintain a targeting of project based Section 8's, especially for special needs housing.

Enterprise supports deregulating efficient PHA's, expanding demolition criteria, and consolidating funding into a public housing capital fund and a housing operating subsidies fund.

However, we oppose the ultimate stages of HUD's proposal to roll public housing streams into the housing certificate fund.

Enterprise supports HUD's proposal to transform the FHA into the Federal Housing Corporation, a Government-owned, market-driven corporation linked to HUD, but freed from its current staffing and regulatory limitations. This proposal contains many features that will improve FHA's internal operations and expand upon its success as a primary mortgage insurer to low- and moderate-income families.

Finally, I wanted to address the home ownership issue, which is also a very important issue, even in New York City, where we have a lot of rental units. Communities throughout New York City see that it's important to have a diversity of housing stock which addresses both the rental market and home ownership market. They like to see an economic mix.

Community organizations have worked with the same partnership bringing in the private sector subsidy dollars through HUD or through the State or city to assist in the development of housing and rehabilitating smaller buildings and making those affordable for home ownership for low- and moderate-income homebuyers.

This has assisted in both providing economic integration and housing opportunities in these communities, and also has brought an opportunity for people to move out of the rental market and out of maybe low-income housing or public housing authorities and into home ownership opportunities without having to move out of the neighborhoods.

Thank you very much.

Senator MACK. Thank you, Mr. Frey.

Ms. Jones.

STATEMENT OF DANETTE JONES, MEMBER-AT-LARGE, BOARD OF DIRECTORS, NATIONAL CONGRESS FOR COMMUNITY ECONOMIC DEVELOPMENT [NCCED]; AND PRESIDENT AND EXECUTIVE DIRECTOR, MADISON PARK DEVELOPMENT CORPORATION, BOSTON, MA

Ms. JONES. Good morning, Senator Mack, and I'm sorry John Kerry left because he is the Senator from my State, the State of Massachusetts, but I did go out to say hello to him.

I am Danette Jones, president and executive director of Madison Park Development Corporation in Boston, MA, and a member of the Board of Directors of the National Congress for Community Economic Development.

On behalf of the community economic development field and the members and leaders of the National Congress for Community Eco-

nomic Development, I would like to thank you for the opportunity to testify today.

We are encouraged that you are seeking the perspectives of community development practitioners on HUD's Blueprint to action.

This discussion and debate is both timely and necessary if we are to ensure that low- and moderate-income people are better served by our Nation's public and private sectors.

We applaud both Secretary Henry Cisneros and the Members of this Committee for your earnest efforts to better serve our Nation's neediest citizens.

The Madison Park Development Corporation is a community development corporation serving residents of the Roxbury community in Boston. Madison Park has been in existence for 28 years and has developed over 500 units of affordable rental housing.

We recently completed a $9.1 million rehabilitation and resyndication of a multifamily housing development, and a $2.2 million rehabilitation of another housing project.

We are a private, non-profit corporation and our success is directly attributable to our ability to leverage private dollars in order to maximize the impact of public investments.

In addition, we're working with our local health center and businesses to revitalize their blighted facilities. In fact, Senator Kerry did participate in a fundraiser for the local health center that we are jointly developing.

The National Congress for Community Economic Development is the national trade association for the community development field with more than 2,000 community development corporations nationwide in its network, and 23 State associations including the Florida and Massachusetts associations who serve as State affiliates to NCCED.

Community development corporations can be found in rural and urban areas of all 50 states and the Commonwealth of Puerto Rico and the Virgin Islands.

We were founded in 1970 and we support our members through information, research, technical assistance, and a capacity building.

According to a nationally recognized census due to be released next month, these community-based organizations have produced nearly 400,000 units of affordable housing, created 67,000 full time jobs, developed 23 million square feet of commercial and industrial space and loaned over $200 million to spur the creation of small businesses and entrepreneurial activities in some of the Nation's neediest communities. CDC's work with community residents to meet local needs and concerns.

As Congress searches for ways to streamline the Federal Government and eliminate wasteful bureaucratic programs, it should keep in mind the proven capacity of these organizations to assist in rebuilding distressed communities.

Rather than adding layers of additional bureaucracy, these organizations return control of the development process to local communities by allowing and encouraging residents of these neighborhoods to address their community problems using market-driven solutions.

HUD's proposals and how HUD plans for consolidating and altering its programs will affect the community development field. The

scope and breadth of HUD's undertaking and its ramifications for the political, social, and economic structures of the Nation reinforce HUD's continued existence as a Cabinet level agency.

I would like to offer some observations which HUD might find useful in its efforts to ensure the attainment of its objectives and possibly diminish any public confusion once it has received legislative approval to implement the Blueprint to action.

The policy areas I will discuss are program consolidation, block grants, local flexibility and performance based standards and housing vouchers.

There are some attractive features of the program consolidation plan. As a practitioner, the notion of dealing with one set of program regulations is quite appealing. In the past, coordinating multiple programs, each with their own distinct regulations, has been frustrating, costly, and time consuming.

Placing these programs under one set of regulations would guarantee that service providers would make more efficient use of existing resources. It is important, however, not to discard regulations which currently ensure that targeted populations receive the benefits they need.

Speaking on behalf of the National Congress for Community Economic Development, I believe HUD deserves to be commended for displaying vision and good faith in its efforts to reinvent itself.

The Blueprint to Action is a thoughtful attempt to address and resolve some longstanding problems that we have.

There must be a way, as HUD looks at block grants, to distribute HUD's funds more efficiently and with more autonomy to States and localities.

But there are some concerns for our field. We're are not opposed in principle to the use of block grants, but we do believe it is important to recognize that, given the proposed reductions in HUD's budget, the conversion of these funds into block grants actually represent a reduction in the resources being provided to low- and moderate-income communities.

If we recondition and overhaul the current service delivery systems, then we should be willing to spend more money in these critical areas.

Our National Association will release a study, as I indicated, next month reporting that the largest source of funding for community development corporations are government block grants. CDC's have used this funding over and over again for community economic development and housing development activities.

Our field does not lack confidence in its ability to access resources under a decentralized system, but the Federal Government should not simply disburse funds and assume that State and local governments will utilize organizations which best serve low- and moderate-income Americans.

For the past two decades, CDC's have devoted a considerable amount of time and energy in educating theFederal system on the value of our work. Consequently, we are deeply concerned about the prospect of losing our forward momentum as a result of too suddenly shifting the entire responsibility for community based development to states and localities. We respect the States. We understand our relationship with them.

NCCED feels strongly that the pursuit of maximum local flexibility should not come at the expense of delivering services to low-income communities. On the one hand, local flexibility often encourages greater public and private capital investments, rewards effective producers, and provides necessary resources to the neediest people and communities.

On the other hand, it may run the risk of expanding political patronage, thereby further disenfranchising low-income residents and opening up local programs to financial abuse.

Performance based standards are a step in the right direction, but while we encourage HUD's efforts to establish performance categories, the implementations of these standards should not result in low-income residents suffering from poorly performing localities, and losing funding for vital services if their city or town fails to achieve the performance standards contained in their local government's consolidated plan.

I agree with the goal of providing those Americans receiving Federal housing assistance with choice and flexibility. All too often, they have been trapped in living conditions which have diminished their quality of life.

As a private owner and property manager of some Federally assisted housing, I am concerned about moving overnight to a universal voucher system. Project based assistance needs to be improved, not eliminated.

Our challenge is to continue to provide incentives for private investment while improving the conditions, potential for development of resident self-sufficiency, and maximizing the public investment in these projects.

In response to the public's demand for increased efficiency and accountability, HUD should examine the use of vouchers as part of an overall national strategy to provide low-income people with affordable housing. But this examination should be undertaken as part of a comprehensive demonstration project in order to better develop performance and cost standards for such housing, and to create an effective process for overseeing and managing this part of HUD's portfolio.

Full scale implementation of a national voucher program, absent any comprehensive prior study, would result in displacing low-income families produce reductions of capital investment in neighborhoods, create cash flow problems for residential property owners and managers, further destabilize neighborhoods and increase the delay of refinancing and rehabilitation projects as investors and lenders reassess their investment and loan risk.

In conclusion, I would like to thank the Chair and Members of the Committee for the opportunity to better acquaint you with our work and our concerns.

I would like to reiterate that there is a network of over 2,000 community development corporations who applaud your leadership, commitment, and resolve to improve the quality of life for our Nation's poorest and most distressed communities.

We stand as a delivery system prepared to implement change, restore faith in Government, empower citizens, and shape a better future for our Nation.

Thank you for your time.

Senator MACK. Thank you for your comments.

I thank all of you for your presentations this morning. Let me begin with a question to all of you.

What is your time restraint?

Ms. DYKSHOORN. I actually had to change my flight so I will be here. Thank you.

Senator MACK. We've heard differing opinions about whether or not the HOME and CDBG programs should be merged or retained as separate programs.

Why should or shouldn't we combine these programs into one block grant?

I'd kind of like all of you, if you would, to reply.

Anybody want to start first?

Go ahead.

Ms. DYKSHOORN. Well, Senator, our executive committee has struggled with this question in terms of how it should be done.

What we were looking at is that the State government, in designing a plan and in developing the consolidated plan that we did do, had to look at all of the various resources, and felt that it would be easier to deal with one block grant combined resource so that you could really develop something that met the various needs that you had in your state, because you do have States that have different housing needs and may have a priority that would place more moneys available in a housing area in a certain part of the State or perhaps more in the infrastructure area.

So we felt that States, in concert with developing with their local communities and developing consolidated plans, should have the flexibility to design, with those available resources, something that works, so you don't take the cookie cutter and say this is how you have to spend your money, but something that is a little bit more flexible.

Senator MACK. Mr. Logue.

Mr. LOGUE. We would propose that there should be a differentiation and separate block grants for community development activities and housing.

I think it really reflects the fact that there are very distinct differences between the two types of activities. And that certainly we are arguing for more flexibility, the most flexibility possible. But there are also good reasons to have discrete funding sources for different and sometimes unrelated activities.

Senator MACK. I might ask you, what are those good reasons?

Mr. LOGUE. Well, the good reasons I think are that it's very difficult to effectively assign a level of funding need, determine a level of funding need for housing activities at the same time you're trying to determine a level of funding need for community and economic development activities.

So, therefore, the measures you would use to appropriate funding and to develop programs would not necessarily be in sync.

If you look also at the existing structure of CDBG funding and allocation, as compared to HOME, which would really be the two models for the separate block grants, you'll see that in CDBG, the eligible participants are nearly a thousand local jurisdictions where in HOME they're much fewer, so you've got a differentiation in who would even be participating in those various block grants.

I think there are reasonable reasons to have some boxes into which we do place money. I think we ought to keep those boxes to a minimum, but there is a distinct difference in determining need and determining how you use funding when you're comparing housing need to economic and community development need.

Mr. FREY. We would think that any block grants should have income targeting requirements to ensure that we're hitting the most needy with the limited resources that are available.

Additionally, we'd like to see a 15 percent set-aside for block grants similar to the HOME set-aside for non-profit community based organizations.

Senator MACK. So what you'd be doing there is creating another box? Is that it?

Ms. JONES. A box within a box.

Senator MACK. What?

Ms. JONES. A box within a box.

Senator MACK. I'm sorry, go ahead.

Mr. FREY. Just seeing that the development itself that is happening and having the most permanent impact in the communities that we've been involved in around the country has been that which has been tied very much to community based organizations working in partnership with the private sector and the Government itself.

Senator MACK. Go ahead.

Ms. JONES. We do support maximum flexibility but I think there gets to be a point where one could go too far. And I think that we would need to have two separate block grants, one focused on community economic development and the other on housing.

You asked the question, why is that.

I think that States really have a lot of pressure these days, especially with the various welfare reform initiatives out there, to produce jobs, jobs, and more jobs, and that if it's all lumped together, there may be the tendency on the part of the State—not Massachusetts of course—to lump it all together and that jobs would get priority over housing.

As those of us who are in the community development field who work as we do in housing and in economic development, we know that viable communities need both.

That I believe is part of the role of the Federal Government to set the broad parameters and say that communities must be achieving on both tracks. And by having those separate pots, I think that's a way for HUD to monitor whether or not that's in fact occurring.

Senator MACK. What about this point that Mr. Frey made, in essence creating his box within the box?

Ms. JONES. Well, I absolutely think it's a wonderful idea from the non-profit perspective.

Senator MACK. I kind of had a feeling you would.

Let me just raise a point and get your reaction to it.

I mean, both of you have pointed out the extreme successes that you have had and one could make the argument that because you have been so successful, wouldn't people, isn't it unnecessary really to have the box?

Wouldn't a State or a local community want you to be involved because of what you've been able to do?

I can see maybe in the beginning, when people were raising questions about, well, are they really going to be able to produce, and the only way you really could get started was by in essence having this set-aside.

But today, wouldn't you be able to argue the success that you've been able to produce really kind of eliminates the need for that set-aside?

Mr. FREY. Let me say, in New York City, again, using that as what I know the most about, we began this program in 1987. At that time, there was not a niche for the non-profit sector to become involved in development.

Since that time, the city, and I believe the State and the Federal Government have learned the importance of that particular involvement, and it's a credible sector that needs to be involved in community development efforts.

It may not have happened unless there was a strong signal from Washington that in the HOME program, it's important that there be a set-aside for non-profit community based initiatives.

So I think that a continual message needs to be sent that no matter what is done in the development area, it's important to touch base and be involved with the non-profit sector.

Ms. JONES. I would echo that sentiment and also say that we have had success. Community development corporations have had success over the past 30 years, but we still have so much work ahead of us.

I mean, if you go to the poorest neighborhoods of this country, urban and rural, you will see that the work has only just begun. And in order to ensure that that work continues, I think it argues that the Federal Government, if it wants that work to continue, has to send a message that the guidelines say this is what we're looking to see, and then the States understand and other localities understand that this is important and that they will do everything within their power to achieve the Federal goal.

By the way, while NCCED has members, I think probably in all 50 States, we only have 23 State associations. Florida and Massachusetts are very progressive. So we've got a lot of work ahead of us in terms of organizing.

Senator MACK. I'm glad to hear you say that.

How do the States feel about that with respect to this 15 percent or this box within the box?

Mr. LOGUE. Well, we have worked effectively in a number of programs with the utilization of set-asides of low-income housing tax credit program and the HOME program have set asides for non-profits. And I think those are levels which we would not argue with. I think we would be concerned if they were any more appreciably increased.

But I think the point is that in many States, and particularly over the last 10 years, we have recognized the need and the good sense to work with non-profits, particularly at the community level.

In Michigan, we allocate much more of our tax credit than the 10 percent set aside to non-profits. We give extra points in award-

ing tax credits to those projects which utilize non-profits, either in partnership or in complete ownership.

We do the same thing in the HOME program. We have been actively facilitating the development of additional non-profit involvement in our housing because we've found that, particularly in urban settings and even in rural settings where the needs for development are most severe, that a community based non-profit involvement helps to assure that you're going to get a better product, a longer lasting product, and an asset to the community that, without them, you would likely not have.

So it's in our best interests. I don't think there's a need to overly prescribe how much of any form of assistance should to go any category of user at the end.

Senator MACK. It sounds like, in a way, though, that you're kind of asking us to establish certain priorities for you. It seems again, if we were to provide the money, that you would do what's in your best interest.

Mr. LOGUE. I would agree with that, but I think our best interest is also the best interest that are being asked to have special set asides. And I think that the, and again the non-profit example I think is a good one for many States.

Senator MACK. Again, what that sounds like to me is you want us to make the political decision.

Mr. LOGUE. No, I would not argue necessarily for any specific set aside. I don't think we would, if you had a 10 or a 15 percent non-profit set aside in any block grant, that would not pose an obstacle to most States, I don't believe. But its need I think is not particularly great either, and I would argue for a maximum flexibility and the least number of prescriptions on how that money should be used.

I would argue to keep, have a few separate boxes but keep those boxes very flexible.

Senator MACK. OK.

Why don't I just toss out another area having to do with match. If we consolidate programs, should we have a match requirement? I'll just toss it out.

Mr. LOGUE. I would argue very strongly that we should not, in an era of diminishing resources probably most likely from the Federal Government and certainly from the State level, to require specific match requirements for any Federal funding flies in the face of flexibility.

If a State's need in supporting a welfare program by using State dollars or other dollars, other match dollars, is the priority, it shouldn't then be required to be used in another setting like housing or community development to meet really what is an arbitrary match requirement.

I would argue very strongly that a match is not necessary and again, maximum flexibility should be the rule.

Senator MACK. Do you have any additional comments?

Ms. DYKSHOORN. COSCDA had also set that in their recommendations.

Senator MACK. Then there's kind of a follow on question that if not, how do we encourage greater participation by the private sector in leveraging of non-Federal resources?

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Mr. LOGUE. I would argue that that is a factual need. It is not something you've got to mandate. In Michigan, when we're doing multifamily housing——

Senator MACK. Can I just hop in for a second again?

Mr. LOGUE. Sure.

Senator MACK. It sounds to me that on the one hand, when I'm asking you about the match, you have kind of one set of responses contradictory to the position that you take with respect to the flexibility.

Mr. LOGUE. I'm not sure I——

Senator MACK. Well, under the match, I want to encourage more funds to flow into housing, which is I would have thought what you would want to have happen.

Mr. LOGUE. Absolutely. I would suggest that that's going to happen whether or not you require a match.

Senator MACK. I'm saying again, back to you, the point that I was making about the boxes, that will happen regardless of whether I provide the box.

Mr. LOGUE. Right.

Senator MACK. We both say we've accomplished the same thing so we'll go on.

Mr. FREY. Senator, I think it's easier to require a match when we're talking about a higher income level. We've seen in housing which has been targeted for lower income households but maybe at 50 to 60 percent of median, that we've been able to bring in private sector dollars as well as tax credit investment on those projects, so there is a match, as well as the city, in its better times, was able to match more significantly.

Where we do find a problem, and maybe this is one of income targeting issue as well, is when you're dealing with very, very low-income housing, and you're dealing with people who are at PA level, public assistance level or below, it's very difficult to bring in private sector dollars or additional match unless you're bringing it in, for example, we are matching even those projects in New York City with tax credit investment, but it's all being set up as a reserve fund for long-term benefits to the project to make sure it can be run as a project for very low-income people for a long-term.

So there is a way to match, but as a reserve as opposed to being a part of the development budget.

Ms. JONES. One of the best things Congress has done, I know in the low-income, primarily minority neighborhood that I work in, is to permanently extend the tax credits and the mortgage revenue bonds. That was real, real important in terms of increasing private investment and the attractiveness of our neighborhoods to private investors.

In addition, I would say the CRA effort is very important towards increasing the attention that the private sector does pay to those neighborhoods where they traditionally do not care to invest.

Senator MACK. Let me raise the question about HUD capacity. One of the concerns that has been expressed is that on one hand, as the new program is being developed, and they are suggesting that they have the performance based funds, we are having a draw down in size and the number of personnel at HUD.

Do you think that HUD does have the capacity to deal with the responsibilities it will have under these new programs?

I'm really kind of directing that to you, Mr. Logue.

Mr. LOGUE. I think there are certainly concerns existing today with their capacity to manage the programs they have, and looking into the future, to manage the programs they would have under just about any of these scenarios.

The fact of the matter is that HUD is not increasing in size and it has no meaningful ability to manage particularly its multifamily portfolio, it's assisted privately owned multifamily portfolio, as we've seen from the FHA problems.

I think that is probably true, although I'm not an expert in public housing, it probably has difficulty dealing with the troubled public housing inventory, and as a consequence, I can only speculate and I would find it hard to believe otherwise, that HUD will continue to have this problem.

When I was at HUD in 1990, my technical services division, which was comprised of 35 people, about 28 of those people were at retirement age or would be in 2 years. And those are people that they just don't make anymore. And certainly, if they do make them, they're not going into Federal service.

That is not to knock the Federal employees at HUD. They are, by and large, a tremendous group of people. They just have too much to do and not enough resources to do it with.

That is most manifest in its inability to really manage its insured housing inventory.

Senator MACK. Let me ask you specifically on the multifamily insurance program, do you think that ought to be phased out?

Mr. LOGUE. I do not think it should be phased out. I think there is a definite role for FHA multifamily insurance. I think for HUD to do it effectively, it has to be a more targeted program and done in conjunction with partners who can perform the jobs that HUD is not capable of performing and probably won't be able to perform and probably shouldn't perform because it's not, the Federal structure is not a good model for overseeing a large multifamily privately owned portfolio.

So I would say, as a good example, the HFA/FHA risk sharing proposal, which we are now into, Michigan's one of the States that's been approved, is a good model for how FHA multifamily insurance can be delivered, where we're taking part of the risk at the State level to do the housing. We are doing all the underwriting, all the management, we have the responsibility, if the project gets into trouble, for working it out. And HUD functions in an almost the pure role as an insurer, but an insurer with a partner they know is going to stay there and be there in good times and bad because that's been our history.

I think with other groups, the GSE's, other State housing agencies, even other good local agencies, there are opportunities to do that type of partnering and really get the Federal Government out of the active, day to day management.

You looked at Michigan, we have, in our agency, a ratio of about 10, 15 to 20 projects per housing management officer, which is probably about the maximum we have overseeing any particular group of projects.

At HUD, that ratio is about 70 to 1. It's impossible for 1 person at HUD to manage and oversee 70 multifamily housing properties, some of which may be in trouble.

When we've got a troubled portfolio, we'll put 1 person on 5 projects. It just can't be done any other way.

Ms. JONES. I would echo some of that too. I serve on the Board of the Massachusetts Housing Finance Agency, and we are now working out a new partnership with HUD relative to 1,200 distressed units that are in HUD's portfolio, multifamily portfolio in Boston, and we're working out the parameters of that now. But it does speak to the State housing agency taking on a more active and aggressive role in terms of managing and transitioning that housing into hopefully resident-owned housing. But in this demonstration HUD has delegated a lot of its traditional responsibility to the Massachusetts Housing Finance Agency.

Similarly, our ratio of staff to portfolio, the Mass Housing Finance Agency portfolio is about 1 to every 17 projects, and we do know that HUD does have this enormous ratio of 1 to 70 or a 1 to 75 ratio that I've heard quoted.

Senator MACK. Ms. Dykshoorn, do you have some comments with respect to the capacity issue?

Ms. DYKSHOORN. I don't have any disagreements with what Mr. Logue has said also in terms of where HUD is at. I mean, we have a good working relationship with them, but I think that they have a great deal of work and are understaffed.

Senator MACK. Well, I think that I am at the point where I would say to you all, I'd be interested if you have one last comment that you want to make to drive a point home, if you feel it hasn't been made.

Anything you'd like to add?

Ms. DYKSHOORN. Senator Mack, I do appreciate the opportunity to be here. I think that the States have an opportunity to make some real differences in terms of how the resources that would be made available to them can also tie in with welfare reform and making some meaningful changes.

We would like the opportunity to be able to do that, and to have resources that are not so laden with requirements and boxes that we have the flexibility to design plans that we feel will work.

Mr. LOGUE. I would just like to emphasize the fact that I think the State role is a very important role in the delivery of housing, and to some extent community development activities, but clearly in housing.

We look to work, as we have been for many years, in partnership with local communities and non-profits and other partners in this.

I would also like, and maybe this was the source of the confusion we had in our discussion, but I'd like to make sure you understand that from our perspective, we do not think that there is a need for set-asides or any particular groups in any of the block grants, including non-profits. I think we can work effectively without them.

The intention of having funding used with other partners, specific partners will be accomplished whether there are set asides or not.

Mr. FREY. I know we have good States on this panel. But I think the other concern that we ought to have——

Senator MACK. You're all very diplomatic.

[Laughter.]

Mr. FREY [continuing]. What the impact is going to be on the capacity of the States to administer to these block grants. Much is being thrown on the States at this point, and we need to be concerned about that nationally. I know that we're all able to take care of it here.

The other thing is I just want to emphasize the importance of not eliminating HUD, the importance that it has for the urban communities that are out there struggling to redevelop themselves.

And we look, with Congress and HUD, to recast the Department as a more constructive partner that will assist in the efforts around the country.

Thank you for inviting us.

Senator MACK. Thank you.

Ms. JONES. I would just say thank you for the opportunity to be heard, and to say that our staff at the

National Congress looks forward to working with your staff around the various proposals that you do craft.

We are pleased to have the opportunity to give input on this very important decisionmaking process.

I would also add that Koya Glaude is here with her father, Steve Glaude, who is the president of the National Congress for Community Economic Development, as part of the take our daughters to work effort, so I did want to acknowledge her this morning.

Senator MACK. Well, good for her, and welcome. We're delighted that you're both here.

Thank you again, all of you for coming. Thank you for your input, and the meeting is now adjourned.

[Whereupon, at 12:20 p.m., Thursday, April 27, 1995, the Committee was adjourned sine die.]

[Prepared statements and additional material supplied for the record follow:]

PREPARED STATEMENT OF STEVE BARTLETT

MAYOR, CITY OF DALLAS, TX, FORMER MEMBER OF CONGRESS

APRIL 27, 1995

Introduction

Mr. Chairman, I appreciate the invitation and opportunity to speak today. I intend to confine my remarks to the city of Dallas and our local perspective on the reinvention of HUD. Hopefully, my background and experience as a former House Member and sitting Mayor and the experiences of the city of Dallas will provide a helpful insight into the HUD reinvention process and complement the testimony of the other scheduled witnesses.

In summary, HUD should be "reinvented" with the following three principles in mind:

1. HUD should be downsized, streamlined, voucherized, and privatized.
2. HUD's focus for the 90's should have a clear and unmistakable emphasis on home ownership for all income levels.
3. HUD programs should lead the way in the devolution of power from the Federal Government to local governments.

These principles have guided the proposals of Secretary Cisneros and are reminiscent of the proposals by former HUD Secretary Kemp. The introduction of market-based strategies, empowerment of the individual and significant roles envisioned for State and local governments should lead to more positive results for America's cities and citizens in the restructuring of Federal urban policy. Reduction of administrative staff which in turn should translate into more dollars for programs is a good step.

The problems and difficulties besetting HUD have been well chronicled. Mortgage loan defaults, rehabilitation needs and increasing subsidies all represent enormous problems to be addressed. Often, HUD has been characterized as bureaucratic with a penchant for micro-management. While these problems are acknowledged, HUD programs have contributed positively to America's communities. HOME and CDBG have enjoyed considerable success in Dallas.

Block Grant Proposals

Consolidation of programs into block grants, the empowerment of low- and moderate-income individuals to make housing choices and streamlining of the agency, included in the Secretary's plans, are all good steps. State and local control of the block grant funds is a welcome relief from Federal micro-management and the one-size-fits all approach which has pervaded HUD policy for 30 years. Performance based measures, if structured properly, can ensure that accountability will be achieved and yet at the same time allow local governments to design and develop programs which are tailored to meet local needs rather than rigid adherence to detailed regulations.

A significant aspect of the Administration's proposals to restructure HUD revolve around this consolidation of multiple programs into block grants. In earlier testimony before the House Economic and Educational Opportunities Committee, I affirmed my belief in and commitment to block grants. Based on my experience as Mayor and as a recipient of categorical grants, I support the efforts to streamline and consolidate the myriad categorical grant programs through the use of block grants. Through this consolidation, the same services can be delivered with more impact and greater efficiency. With the appropriate formula and authorized flexible uses, block grants represent a superior methodology compared to categorical grants.

The keys to development of effective block grant legislation are: (1) a precisely defined legislative policy regarding purposes and eligible uses and; (2) adoption of a formula to carry out the policy. The formula components must be readily verifiable from information already available to the Federal Government and relate directly to the incidence of the problems being addressed. With "fuzzy" data, the formula will be subject to manipulation and results will be correspondingly skewed.

A block grant program, to achieve its purpose, must allow enough flexibility for the recipient to tailor programs to achieve the desired results in a local community setting. Communities vary across the country. What works in Dallas, Texas may not work in Philadelphia, Pennsylvania or Boise, Idaho and the converse is also true. I am encouraged that the Secretary's proposals seem to reflect this tenet.

The specifics of the performance measurements, as set forth by the Secretary, are critical; the "devil is in the details." Performance goals should not be a guise for micro-management. The whole spirit of block granting is local control. Through the use of new and emerging technologies, including modems, wire transfers, Internet,

etc., paperwork and reporting requirements can be minimized. Waivers for local conditions should be afforded. Funds for administration should always be allowed, although it is reasonable to cap or otherwise limit them,

Flexibility and accountability in the consolidated HUD programs require a delicate balance. License can not be given to repeat the past problems. Accountability is made more difficult by the anticipated reduction in HUD staff. Yet, a strictly defined approach will stifle innovation. The current CDBG program represents one alternative. A minimum national goal of a certain benefit to low- and moderate-income individuals with freedom in meeting those goals, has for the most part worked well. Approval of the plan by HUD, after public input and consideration, would ensure accountability. As a second alternative, the current welfare reform waivers could serve as a example. Local governments could apply for a waiver of laws and regulations necessary to implement a program. These programs serve as a model for accountability and flexibility. Local elected officials would be held accountable for their actions. Public reports of the activities and expenses would be published annually.

While the block grant approach is a positive step forward and one which the Senate should seriously consider, even block grants can be over-regulated The Committee should not perpetuate these regulatory burdens in the HUD restructuring. Some of these burdens are illustrated in the discussion on the CDBG and HOME block grants. Other specific burdens are discussed later in my statement.

Two Case Studies: City of Dallas Block Grant Experience

The Secretary proposes to fold CDBG and a number of other existing Federal programs into one block grant designated as the Community Opportunities Fund HOME becomes the basis for the Affordable Housing Fund in the Secretary's proposal. Since these are the programs with which local governments are most familiar and form the basis for two of the proposed consolidated block grants, it is appropriate to review the implementation of these programs.

Community Development Block Grant Funds

The city of Dallas will receive approximately $20 million this year through the Community Development Block Grant program. Local governments across America support and applaud this program and look forward to its continuation as part of any HUD restructuring.

In particular, Dallas emphasizes the need for predictability and flexibility in a revamped CDBG program. CDBG funds can currently be used for a wide range of activities: Housing assistance, economic development, public services, and physical improvements. The scope of eligible activities should remain broad in order to provide local governments with the maximum opportunities to devise strategies tailored to local needs. The Secretary is right to continue the formula allocation at 70 percent for local governments and 30 percent for States.

The city is taking positive steps with CDBG and considers it a successful program. Having said this, the program is subject to requirements which make administration more difficult and expensive. Following are some examples:

- *Economic Development.* The use of CDBG funds for economic development activities designed to benefit CD approved areas is constrained by regulations. The CDBG program allows local governments to aggressively pursue long term, area wide economic development. Required is demonstration of actual job creation within 24 months. This is not always feasible when considering the tire and costs related to economic development or redevelopment of an area. The expansion of applicability of the area benefit objective should be encouraged. Activities which would fall into this category include pre-development costs, area specific market studies, infrastructure improvements of commercial land, improvements of commercial properties, and redevelopment of economically distressed areas.
- **Regulations.** The regulations governing HUD programs are complex, ever changing and compiled in several places. Pertinent regulations can be found in 24 CFR Parts 91, 570.301, 135, 58, 570; OMB Circulars A–110, 128, 133, 87, and A–122 and 29 CFR for Labor Standards such as the Davis-Bacon Act, Copeland Act, Fair Labor Standards Act, and Contract Work Hours Safety Standards Act. Note that these represent the number of regulations for a block grant, which is intended to be flexible.
- **Formula.** The formula used for CDBG distributions works to the disadvantage of the certain cities and should be revised. I note that my friend, Mayor Steve Goldsmith of Indianapolis, commented on this need in his prior testimony before this Subcommittee. The formula presumes that housing of a certain age is in need of Federal assistance. The formula ignores the variations in housing stock across the country and consequently favors certain areas over others. The communities

faced with deteriorated housing need to be assisted equally, based on the physical condition of their environment, and not simply based on age as currently written.

HOME

The HOME program is a block grant which I believe has worked well for the city of Dallas. The city strongly supports its continuation as part of the consolidation of HUD programs. It can be the backbone of an affordable housing effort and numerous other programs can be eliminated. The city supports the continuation of the ability to use funds for new construction and not just rehabilitation.

Monies are distributed directly to the city of Dallas and other local governments through a formula which recognizes the age of housing stock, income levels of the targeted population and other factors. The city of Dallas will receive approximately $6 million through this program. The funds are available for construction, reconstruction, infrastructure development related to housing and other housing related uses.

As with CDBG, the greatest attribute of the HOME program is that it allows creativity in local program development. Block grants allow greater leveraging of private sector resources and involvement because locally crafted programs can be structured to take advantage of local opportunities. Some particular successes in Dallas are:

- Development of a Capacity Building Program for nonprofit housing producers. The city of Dallas set aside approximately $600,000 to be used over a period of 3 years to increase the ability of community-based organizations to create housing.
- The city funds a revolving loan fund for housing. The fund has served as a source of reduced financing for affordable housing rehabilitation and development. The city leveraged over $50 million for affordable housing mortgages through a consortium of 12 banks using this program.
- Using less than $500,000 of HOME funds, the city of Dallas assisted 254 families in home ownership. Over $10 million was leveraged through the "Up-Front Cost Assistance/Mortgage Assistance" program.

Specific, unnecessary regulations which hinder the implementation of the HOME program are:

- HOME regulations require annual, onsite inspections of multifamily properties and income verifications of tenants by city personnel to ensure housing quality standards and affordability requirements are met. Deed restrictions, financing conditions, and other requirements are sufficient to enforce affordability requirements without city annual involvement.
- Specifically, in a multifamily rental context, affordability standards and requirements should be simplified. The regulations are so confusing that the auditing firm hired to conduct the required Single Audit, had several days worth of trouble trying to understand the regulations themselves, let alone determining compliance by the city.

A number of administrative hurdles are common to the HUD CDBG and HOME programs. Following are some of the common issues:

- **Eligibility Criteria.** The income eligibility limits for major grant programs varies from 50 percent to 60 percent to 80 percent of median income depending on the specific program. Standardized income limits would provide for one-time qualifying and uniform eligibility for all programs allowing for more consistent assistance. Eligibility, defined in terms of low, very low, and extremely low populations (80, 50, and 30 percent of median) is continually being redefined by HUD and is a source of confusion.
- **Audit Requirements.** Regulations require that an audit be performed on subrecipients receiving more than $25,000 in a fiscal year. Each of these audits costs $1,000 to $4,000. Often, the same subrecipients receive grants because of satisfactory performance. Likewise, the same audit requirements apply to a $10 million grant and a $25,000 grant.

Public Housing

Public housing is the most over regulated part of HUD. Empowerment of public housing residents is key to the meaningful modification of these programs. Increased use of vouchers to give individuals the freedom to choose where they live will drive demand for better low- and moderate-income housing and should improve the existing public housing developments.

Elimination of operating subsidies and replacement with vouchers dedicated to rental assistance shifts the focus to creation of demand for decent affordable housing. The ability to make housing choices will force the PHA to compete for tenants and introduce significant new positive dynamics into the public housing equation.

Public housing residents will no longer be forced to endure dilapidated residences and lethargic and indifferent PHA's will upgrade or cease to exist.

Specific Restructuring Points

Reform of HUD should not be viewed in a vacuum. At this time, when old ideas are being challenged and programs and agencies are being reviewed, the mission of HUD must similarly be scrutinized. I would suggest that the Subcommittee consider reform of HUD and its policies and programs in conjunction with the Senate welfare reform effort. In this way, an integrated and holistic approach to the needs of low-income and moderate-income individuals can be comprehensively addressed. In particular, public housing should be reviewed with this in mind. The following are some examples of steps which could be adopted.

1. *Use of vouchers for downpayment and mortgages in addition to rental assistance.* In addition to rental assistance, vouchers could be used for mortgage payments. Encouragement of resident ownership of public housing should remain a goal.
2. *Time Limit.* Originally, public housing was intended to be a "helping hand." Over the years, public housing instead has become a way of life and symptomatic of a lifestyle often devoid of hope. A PHA should be empowered to impose a time limit on vouchers. Voucher recipients would be "graduated." PHA's would in turn receive the voucher funds back for additional vouchers.
3. *Enterprise Zones.* The empowerment zone/enterprise community program was recently implemented. Over seventy-five local governments competed for designation as one of six urban empowerment zones and the $100 million grant which accompanied *each* designation. In reality, it was too much money for too few jurisdictions. Sixty-five communities, including the city of Dallas, were designated urban enterprise communities. Grants of approximately $3 million over 10 years are authorized for each enterprise community designee.

This program has little similarity to the original enterprise zone concept.

The city of Dallas has used enterprise zones effectively without Federal assistance. The zones are designated according to poverty criteria. Businesses locating within a zone are eligible for property tax cuts. This is the sole benefit. There are no grants. Successful programs similar to these are in operation throughout the country. As you can see, these programs and zones bear little resemblance to the Federal initiative.

A successful enterprise zone program incorporates two principles:

1. The designation must be as close to self defining as possible. With self authorization, the grantsmanship pervasive in the implemented program is eliminated; and
2. The businesses which locate in the zones should be eligible for tax incentives, not Federal grants.

This is a real, meaningful approach, which results in a win-win-win for the Federal Government, local communities, businesses and disadvantaged individuals compared to the empowerment zone "lottery" created last year. With these tax incentives, the bill would still likely be revenue neutral. As opposed to the enacted empowerment zone programs and the expenditure of billions of dollars in grants to just a few communities, businesses across the country could be expected to create jobs in the self-authorized areas. The Federal Government would enjoy increased revenues. Individuals who likely would have few employment opportunities and little income would instead have a job and pay income tax.

I suggest that the current empowerment zone/enterprise community program be scrapped. It should be replaced with:

1. Self-authorized zones based on concentration of poverty in census tracts; or
2. Take all the empowerment zones and enterprise communities and designate them as enterprise zones.

Businesses locating within the zone would be eligible for tax incentives, such as 0 percent capital gains and 0 percent payroll taxes.

Following are specific points which I suggest be included as part of any HUD restructuring. Included are several particular proposals of the Secretary which deserve implementation.

(1) A true restructuring has not taken place without a review and repeal of the current regulatory barriers. The current proposals make no mention of any such wholesale review and rollback of regulations. This review can be conducted in one of two ways. First, a sunset review of regulatory barriers regarding barriers on local governments and PHA's could be undertaken. Those regulations which were not reauthorized within say 3 years would be eliminated. Second, a Commission could be

appointed, much like the base closure commission, to review and recommend modifications to the current regulations.

As previously pointed out, problems exist with the current CDBG programs which should not simply be continued and passed down through a consolidated block grant. Besides these modifications, the following restrictions, which I recommend be remedied as part of any HUD restructuring, include:

a. *Elimination of the one-for-one replacement policy.* Under current policies, public housing units must be replaced one-for-one if demolished. This policy results in the continued deterioration of housing stock and traps residents living in the affected developments. Deteriorated housing stock with high vacancies have been the result of this policy. Demolition must be allowed to proceed.

The Senate rescissions bill moves toward eliminating this policy and the Secretary proposes to remove this impediment.

b. *Davis-Bacon Repeal.* Repeal of Davis-Bacon would yield the largest foreseeable impact which could be enacted. The city of Dallas is pleased to see the legislation sponsored by Senator Kassebaum which would repeal the Davis-Bacon Act. Elimination of this Act will result in the savings of reduced project costs and savings in administration for the city of Dallas. Davis-Bacon is an impediment to the hiring of low-income, unskilled apprentice level workers and small minority contractors. A contractor can not afford to pay the Davis-Bacon wage rates and also teach a young man or woman a trade which they in turn can use to bring themselves out of poverty. Small contractors, many of them minority, do not bid Davis-Bacon projects. The administrative burdens are too great. As a result, larger contractors typically receive awards of Davis-Bacon affected contracts. If, rather than eliminating Davis-Bacon, the threshold is raised, then a bare minimum of $250,000 should be adopted.

c. *Public Housing Eligibility for Section 8*—Regulations currently give preference for Section 8 vouchers to those on a waiting list for public housing. Since there are more individuals on the waiting list than vouchers available, those individuals in public housing who might want a voucher are denied one. This procedure has effectively imprisoned those in public housing.

d. *Rent Income*—I am pleased that at least one particular burden is subject to rollback. I note that the Secretary is interested in removing the requirement that a tenant of public housing pay at lest 30 percent of his or her income as rent. This removes a disincentive for individuals to find work.

(2) The Secretary has proposed that FHA remain under Government control. Rather than a Government corporation, FHA should be privatized. The focus of FHA should be directed to high-risk homeowners with an emphasis on first-time and inner-city homebuyers.

FHA has worked wonders for the suburbs surrounding America's center cities. At the time that these urban frontiers have boomed, the center city has declined. An FHA which is focused on first-time and inner-city homebuyers would do much to reverse this tide and bring individuals back to the center city. Indeed, one of the intended goals of the Affordable Housing Fund is to draw moderate-income families back to or help stabilize distressed communities. The FHA, with a specific focus on this goal, would be a powerful ally in the effort to lure these individuals back to the center city.

I note that the Secretary is opposed to privatizing FHA and makes a number of arguments for its continued operation as a Federal agency. Currently, FHA funds are available to rehabilitate single-family housing but the program is underutilized. In any revamped HUD, this program should be emphasized and strengthened.

(3) The Congress should develop a sound formula for distribution of the block grant monies. The formula criteria should reflect the differing demographics throughout the country. I have already discussed the revisions needed in the CDBG formula. In addition, a formula based on pockets of poverty rather than wholesale poverty will allow funds to be targeted throughout the country in a more individualized fashion. Individuals need the assistance whether they live in an area of wholesale poverty or only in a pocket of poverty within a more affluent area.

(4) The Secretary's proposals contain several new mandates particularly with respect to specific "special populations." "Set-asides" which focus on special populations are unnecessary and will result in intrusion by HUD into local affairs. What sounds like concern and regard for affected populations could turn into HUD micromanagement. Innovations will be stymied.

This special attention is unnecessary. These special populations are often quite active and well represented in local government and are able to make their desires

known. Local elected officials who ignore the groups do so at their peril. The local political process is quite sufficient to ensure that their needs will be address.

Conclusion

In summary, I believe that:

- The consolidation and use of block grants, as proposed by Secretary Cisneros, is a good start in restructuring HUD. The HUD reinvention should focus on these three principles:

  1. HUD should be downsized, streamlined, voucherized, and privatized.
  2. HUD's focus for the 90's should have a clear and unmistakable emphasis on home ownership for all income levels.
  3. HUD programs should lead the way in the devolution of power from the Federal Government to local governments.

- All the problems will not be solved through the use of block grants. Many block grant programs themselves are over regulated. Formulas should be modified. Congress should encourage maximwn flexibility to promote maximum innovation and meet local needs. Current restrictions must not be simply passed down to local governments.

Summary

With old ideas and methods being challenged, it is time for a serious reevaluation of HUD and its programs to be undertaken. The Secretary has made a good start in proposing consolidation of programs into block grants and empowering recipients of HUD programs. In the reinvention of HUD, the empowerment of individuals should be of great significance. We have seen the results of the last 30 years. It is time for a dramatic change.

HUD should be "reinvented" with the following three principles in mind:

1. HUD should be downsized, streamlined, voucherized, and privatized.
2. HUD's focus for the 90's should have a clear and unmistakable emphasis on home ownership for all income levels.
3. HUD programs should lead the way in the devolution of power from the Federal to local governments.

Consolidation must be accompanied by the proper formula which allows for flexibility in tailoring the use of the funds to meet the needs of communities throughout the country. Flexibility and accountability in the consolidated HUD programs require a delicate balance. License cannot be given to repeat the past problems. Accountability is made more difficult by the anticipated reduction in HUD staff. Yet, a strictly defined approach will stifle innovation. Models which might be used include:

1. The current CDBG program.
2. Welfare reform waivers.
3. These programs can be a model for accountability and flexibility.

HUD restructuring should be considered as part of welfare reform. So often the problems of those on welfare encompass the kind of services which HUD has traditionally delivered such as public housing. I would urge replacement of the current empowerment zone proposal and its emphasis on grantsmanship with adoption of a program which includes self authorization or designation of enterprise zones and delivery of tax incentives, such as 0 percent capital gains and 0 percent payroll taxes for businesses locating within the zones. Similar programs based on property tax abatements have worked well for Dallas and other communities throughout the country. To encourage home ownership, vouchers could be used for down payments and mortgage payments on homes. Finally, PHA's should be empowered to limit the time residents may use vouchers.

The creation of block grants is not without its problems. Current block grants have their share of over-regulation. The current programs should not be block granted and passed onto local governments without a thorough review of the difficulties inherent in the existing block grants. Specific issues include:

1. Repeal of Davis-Bacon.
2. Privatization of FHA with an emphasis on first-time and inner-city homebuyers.
3. Revision of formulas.
4. The elimination of set-asides for special populations. The potential for HUD micro-management is great.
5. A different scheme for the allocation of Section 8 vouchers to public housing residents.

6. Elimination of the requirement that a certain percentage of income is devoted to rent.

PREPARED STATEMENT OF RICHARD C. GENTRY

EXECUTIVE DIRECTOR, RICHMOND REDEVELOPMENT AND HOUSING AUTHORITY, VA

APRIL 27, 1995

Good morning, my name is Richard C. Gentry. I am executive director of the Richmond (VA) Redevelopment and Housing Authority. For purposes of my testimony this morning, you should know that I have also been the executive director of the Austin (TX) Housing Authority and prior to that the director of operations of the Greensboro (NC) Housing Authority. Also, I currently serve as senior vice president of the National Association of Housing and Redevelopment Officials (NAHRO). NAHRO is a 62-year-old national professional association representing over 9,000 practitioners in the fields of housing and redevelopment nationwide. Consequently, I speak to you this morning not only based on my own 23 years of experience, but also based on information gained by networking with colleagues around the country.

Secretary Henry Cisneros and the Department of Housing and Urban Development (HUD) should be applauded for the most positive benefit of the HUD Blueprint which was to completely open up the debate concerning the future of our programs. Rather than approaching program improvement from the basis of tinkering with current programs, the Blueprint proposes major reform and has set the stage for many of the proposals which are before you during this period of your deliberation.

Unfortunately, the HUD proposals for the public housing program, which is slated for the most major change, are flawed in that these proposals continue to call for a uniform, mandated "cookie cutter" approach to the programs of 3,400 housing authorities. Many of the problems we face today are the result of a program which is built on the HUD-mandated notion that one size fits all. Market conditions, housing stock conditions, housing needs, program size, and profile vary across the country among the various local programs.

The conversion of public housing to vouchers would work in some localities, but is unworkable in others. In any event, the notion that a program flawed by the dysfunction of a centralized, top-down design can be cured by the imposition of another centralized, top-down design is simply wrong. The Blueprint assumes that the existing public housing program does not now meet the market demand in communities around the country. If this is true, why are there over 1 million families on the waiting list for public housing? Also, recognizing this demand for the current stock, why put that stock at risk of being lost because it is not, in all cases, competitive with private sector housing?

Let me be more specific on this subject of public housing competing in the marketplace. The program was designed and deliberately precluded by HUD regulations from becoming competitive for most of its 55-year history. In the past, HUD regulated the size of units, the amenities permitted, the design, the admission process, and many of the factors which would have permitted public housing to be competitive.

Today, however, things have changed and housing agencies are permitted to develop public housing on a scattered site basis which is indistinguishable from neighboring private sector units.

In each of the communities which I have served, there are developments which fit the first category I described. While modernization of those units will improve their quality, they will still not be on a level playing field with many private sector units, yet they do provide decent and sound housing for low-income Americans. Further, there is the argument regarding which option provides the maximum economic value to the taxpayer. We have a $90 billion investment in the public housing program and there are over a million units to show for that investment. Those units are providing housing for a population which desperately needs it. Additionally, according to a paper produced by the Senate Appropriations Committee late last year, the current Section 8 program is significantly more expensive to the taxpayer than is the public housing program. The difference is approximately $2,000 per family, per year. Accordingly, if public housing is voucherized, it is highly likely that either fewer families will be served or more Federal funding will be needed, while existing public housing properties will be neglected.

Let me give you another example. Assume a development of 200 to 250 units was built 30 years ago. All of the families receive vouchers and despite some renova-

tions, between 25 and 50 families decide to move and are fortunate enough to find units within the locality. The housing authority is left with a development with a 20 percent vacancy and due to concentration in one location, size of units, etc., the agency is unable to rent the units without subsidy. The cycle of deterioration is set in motion. Vacant units attract crime, more vacancies and the development ends up becoming troubled and has to be demolished. The result is the community has lost 250 sound units which should have served not as permanent housing but a "way station" for families on their road to self sufficiency.

The Office of Management and Budget, in the past, has complained that the Section 8 Certificate program has artificially inflated the rental market because landlords learn the system and maximize the rents they charge. What will happen with an additional 1,400,000 certificates in the market? The cost of certificates or vouchers is more expensive than managing public housing when you consider the cost of managing after the playing field has been leveled with modernized and "competitive" units.

The public housing program offers the prospect for a continuum of programs and options leading up to the goal of homeowner status for particular families. Many of the 15–20 percent of families currently moving out of the program today, move into home ownership situations. In most of these cases, these are families who will not return to the public housing program.

My approach for addressing the issues surrounding the public housing program which the HUD Blueprint misses is to create a program which allows maximum flexibility at the local level. For those communities where the HUD model works, let it work. But for others, let the local agency design a system which is tailor-made to the circumstances of the individual community and its needs. In either case, devolve authority to allow the community to decide.

This approach is best addressed in the proposals put forward by NAHRO, an agency I represent as senior vice president. For your information and use, I am attaching a comparison of the NAHRO proposals vs. the HUD Blueprint. You should note that the NAHRO proposals provide the maximum chance for localities to fully realize the potential of our programs at the local level as a result of the built-in ability to adapt the programs to local conditions. You should also note that these proposals cover the entire range of housing and community development programs at the local level. The NAHRO proposals also reflect the concept of local decision-making applied to each of the programs.

The flexible approach is also advantageous in this current environment because it permits a local agency to design a program which can accommodate some of the funding cuts being considered by the Congress. It would also allow the locality to develop a more balanced program reflecting not only reduced funding but also the needs of the community. For example, residents are currently burdened by a dysfunctional, counterproductive rent system, mandated by Federal law, which punishes residents who work. Local flexibility would give us the opportunity to design and implement a reformed rent system which would reward our residents for productive behavior. The key is that we are professionals at the local level and we can design and administer a program which addresses the needs of our communities. We also are responsible to a Board of Commissioners, locally appointed who have the responsibility of developing policy to address local needs. Allow us to adopt our programs to fit at the local level, reflecting broad public purpose and goals established at the Federal level.

Before leaving the subject of public housing, let me point out one of the common elements of all current proposals which is to quickly and decisively address troubled public housing, the deteriorated, obsolete, and unacceptable properties that exist in some communities today. Demolish this drain on the program, its resources and its reputation. These units which might number up to 100,000 should be demolished immediately with no requirement for replacement except for those units which might be occupied. Also, those chronically troubled housing agencies should receive direct forceful action to reverse their performance, including the possibility of judicial receiverships or other forms of alternative ownership and/or policy setting.

The magnitude of the changes proposed to the public housing program and the limitation of time force me to focus on the public housing reforms I believe should be addressed by your Subcommittee. Other programs which my agency administers, including Section 8, housing development, and CDBG should also be modified to provide better and more effective programs at the local level. Time does not permit me to go into detail on those programs at this time. I do however, refer you to the NAHRO proposals which comprehensively address these other programs.

NAHRO PUBLIC HOUSING PROGRAM: COMPARISON 3/30/95

NAHRO PROPOSAL	HUD BLUEPRINT
o Program administered by local housing authorities (LHAs).	o Same
o LHAs determine the mix of household incomes, but serve primarily 80% below MSA median. Units receiving federal subsidy required to house residents at 80% or below. Any units serving residents above 80% would not be eligible for federal subsidy.	o During the transition phase(Stage I), there appears to be a an income eligibility cap at 50% of MSA median. After transition, LHAs will be allowed to give preference for up to 50% of admissions to families working toward economic independence and will tie other preferences to the Comprehensive Plan focussing on those with severe rent burdens. During Stage II, families with incomes up to 80% of MSA median may be admitted. In Stage III all residents would receive certificates. However, to protect the stability of elderly, developments, all elderly residents would receive their certificates based on a schedule, so that as people with certificates move out new residents would move in to help keep the building occupied and stable.
o An agency plan is required annually in order to receive the federal formula block grant. The plan would be developed with local input and be the subject of a public hearing. Each agency would certify to HUD that it has a plan that addresses theses basic elements: 1- Mission statement 2- Eligibility, admission and Occupancy requirements 3-Management plan 4-financial statement/operating budget 5-modernization and maintenance plan 6-Performance measures 7-Rent structure.	o HUD has no such agency plan and retains several requirements that the NAHRO proposal would leave to local flexibility.

NAHRO PROPOSAL	HUD BLUEPRINT
o LHAs will determine appropriate rent structure. Rent would no longer be limited to a 30% rent to income ratio. Flat rents, tiered rents, rent based upon a percentage of income, minimum or ceiling rents, market rents for some units, or various combinations.	o HUD would permit LHAs to adopt ceiling rents and to make their own program of rent deductions for working families.
o Block granted funds would be distributed to LHAs. In FY 1996 funds for existing programs, including operating subsidy, modernization, plus TOP, FIC, MROP, Drug Elimination Grants, Service Coordinators, Congregate Housing and Early childhood Development, if funded, would be consolidated. All activities from these programs could be eligible. The formula used to distribute the funds would be based on the amount received under the current modernization and PFS formulas, plus a prorated amount on a per unit basis from the total of the other consolidated funds. A new formula to distribute block grant funds to all LHAs would be developed and refined for implementation in FY1997.	o HUD has three stages. During Stage I, existing public housing funding programs would be consolidated into two block grants: the Public Housing Capital Fund, which includes HOPE VI funds/sites whereas the NAHRO proposal does not, will have a formula that will be split between backlog and accruing modernization needs, but weighted more heavily to backlog; and a Public Housing Operating Subsidy Fund There is also a set aside for tenants. During Stage II, the block grant would be abolished and units would receive project Based Certificate funding, then finally during Stage III, the residents would receive the Certificates and there would be no direct funding to LHAs at all anymore.

NAHRO Public Housing Program: Comparison

NAHRO PROPOSAL	HUD BLUEPRINT
o The LHA would be required to operate subject to four federal performance goals, which would have to be included in each agency's plan. In addition, the LHA will develop local performance goals and objectives to be approved by their local boards.	o HUD would continue to use PHMAP.
o Decisive action would be taken regarding troubled housing authorities and severely distressed housing. HUD would be required by statute to appoint a receiver to operate a troubled LHA without local or state interference. While in receivership a comprehensive plan will be developed in concert with the LHA, the community and residents. Industry technical assistance teams will recommend whether the existing LHA should continue to operate in its present form.	o HUD would also seek statutory requirement to find LHAs in breach of their contract and says HUD must administer the LHAs in breach, appoint a conservator, or seek a court appointed receiver
o Small housing authorities would be included in all formulas for funding. Both operating subsidy and modernization funding needs of small agencies will be included in any formula distribution system developed.	o HUD would also include small LHAs in formula funding. HUD is planning to "voucher out" all LHAs with under 100 units by 1999, all with under 250 units by 2000, all the rest by 2002.
o NAHRO proposes the elimination of federal red tape by proposing federal and regulatory modifications:	o HUD would have federal procurement supersede state and local procurement and also retains the following requirements:

3

NAHRO Public Housing Program: Comparison

NAHRO PROPOSAL	HUD BLUEPRINT
o Abolish the allocation plan requirements for the elderly and disabled.	o Does not address allocation plan, but does give priority to elderly and disabled very low income applying for units designated for elderly/disabled.
o Abolish one-for-one replacement rule.	Retains first right to purchase to tenants in demo dispo
o Modify site and neighborhood standards.	o Does not address
o Abolish the Brooke amendment.	o Does not address
o Abolish federal preferences. Replace with locally developed preferences that comply with fair housing requirements.	o HUD would permit LHAs to have local preferences for up to 50 % of admissions to families working toward economic independence and to tie other local preferences to the Comprehensive Plan. There would also be a preference for low income elderly and disabled for elderly/disabled buildings.
o Abolish lease and grievance procedures. Replace with local landlord tenant law except in states where there are no due process provisions	o Retain lease grievance regs during transition phases.
o Increase the threshold for Davis-Bacon and, reduce the paperwork requirements to ensure the effective and efficient use of funds.	o Does not address

4

NAHRO Public Housing Program: Comparison

NAHRO PROPOSAL	HUD BLUEPRINT
o Eliminate the Public Housing Management Assessment Program (PHMAP). Replace with required federally established result oriented goals and locally developed performance measures and management plans.	o HUD would continue to use PHMAP
o Eliminate unfunded mandates (FSS, Section 3).	o HUD retains both FSS and Section 3 requirements
o Revise the Annual Contributions Contract and the deeds of trust on public housing property. Allow LHAs the flexibility to implement their locally developed plan.	ACC restrictions for low income use of public housing o HUD's role will shift from its current emphasis on monitoring and compliance to technical assistance.
o HUD's role will shift from its current emphasis on monitoring and compliance to technical assistance.	

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NAHRO TENANT-BASED RENTAL ASSISTANCE PROGRAM (TBRA) COMPARISON

3/29/95

NAHRO PROPOSAL	HUD BLUEPRINT
NAHRO proposes that all eligible rental assistance activities under Section 8 Certificates, Vouchers, McKinney, and HOME be consolidated under one flexible, rental assistance program block grant to Local Housing Agencies (LHAs) to provide housing assistance to households up to 80% of median income using private and public sector housing.	Consolidate all current public housing, assisted housing, and Section 8 rental assistance programs into one "certificate fund" (Housing Certificate Fund -HCF), administered by LHAs. HCF will be targeted to households up to 50% of area median income.
The NAHRO program proposal eliminates federal preferences and federal set-asides for special populations and allows flexibility for each locality to design their program to meet the needs of people in their community.	Elimination of Federal Preferences, allow targeting up to half of units to admit families defined with "urgent housing needs" as described in consolidated plan and the other half for working or families working toward economic independence. Require at least 10% of recipients be taken on a first-come, first serve waiting list. Income targeting rules will apply. Prohibits local residency requirements. Allow special purpose waiting lists for homeownership to include families with incomes up to 60% of area median income. .

NAHRO Tenant-Based Rental Assistance Program (TBRA) Program - Comparison 2

NAHRO PROPOSAL	HUD BLUEPRINT
The NAHRO proposal offers extensive deregulation by eliminating the following federal requirements in the TBRA program: o Rent-to-income caps (Brooke Amendment), o Fair Market Rents (FMRs), o Administrative fee based on FMRs, o Portability, o Waiting lists, o Lead based paint requirements, o Family Self Sufficiency, o Federal preferences, o Public housing residents maintaining federal preference on Section 8 waiting list (Bartlett Amendment), o "Take-one-take all" owner requirements, o Endless lease, o Damage and vacancy payments, o Landlord 90-day notice for termination of contract.	Additional administrative funds provided to LHAs for subcontract for counseling, housing search assistance, and recruiting landlords. LHAs will be required to use a portion of turnover and incremental for spacial deconcentration moves. Performance bonuses and increased flexibility to participate in metropolitan mobility strategies. Eliminate take-one-take-all, endless lease, 90-day notice for owner, and prohibition against lease termination for good cause. Families evicted for serious lease violations will lose their assistance.
LHAs administering this program will be required to develop an Agency Plan which contains the following basic elements: eligibility, local preferences, rent levels, relationship to locally accepted community designed plan, tenant payments, and voluntary self-sufficiency efforts.	LHAs will be required to develop a strategy for the local utilization of HCF resources, to be incorporated into consolidated plan for locality or State. LHAs will be permitted to transfer up to 15% of HCF funds to AHF for project-based operating subsidies targeted to very low-income.

NAHRO Tenant-Based Rental Assistance Program (TBRA) Program - Comparison 3

NAHRO PROPOSAL	HUD BLUEPRINT
Rent standards will be set by the local LHA and could vary by neighborhood, locality, or area of jurisdiction to ensure affordability and promote deconcentration.	Continue HUD-established Fair Market Rent (FMR) requirement but set based using 40th percentile. LHAs will be permitted to use either HQS or substitute local code.
Tenant Payments will be set by the LHA and can be used as an incentive for self-sufficient efforts to encourage training and employment. Methods could include fixed subsidy amounts, creating minimum tenant payments, adjusting the percentage of income paid toward rent, or some graduated increase in tenant payments as an incentive for working families as income increases.	LHAs could adjust definition of income used for calculating rent (exempting a portion of employment income or providing deductions for work-related expenses) as incentives to working families. Subsidy will be calculated on the basis of HUD-determined FMR at 40th percentile.
All tenants will be required to sign a Tenant Contract with the LHA as a condition of receiving housing assistance. Contract to include subsidy amount and conditions for subsidy and term limits (if implemented), reasons for termination or extension; conditions of any self-sufficiency plan; sanctions for noncompliance; and security deposit requirements.	Require nonworking, able-bodied residents to perform a minimum of 8 hours of community work. Exemptions for elderly or severely disabled, or who already meet welfare work requirements. "Shoppers incentive" will remain allowing families to receive a reduction in their contribution to rent if they select units less than FMR.

NAHRO Tenant-Based Rental Assistance Program (TBRA) Program - Comparison 4

NAHRO PROPOSAL	HUD BLUEPRINT
<u>LHAs can use the TBRA program to support local self-sufficiency efforts to reduce reliance on welfare and other public assistance</u>. A program component can be a "phase-out" of housing assistance with exemption for select groups, such as elderly and disabled.	LHAs will be permitted to make adjustments to rent and subsidy levels to honor pre-existing commitments, (FSS, project-based contracts under HOPE-VI plus program, etc.)
The Tenant-Based Rental Assistance program will <u>utilize national performance goals</u> based on NAHRO's Key Principles and modeled after other federal block grants that stipulate broad federal program goals. Program goals should include: serving households below 80% of area median, establishing a financial management component, and creating program utilization performance criteria. Verification of compliance with the plan will be based on meeting the federal program goals in the agency plan, being accountable to the agency board, and coordinating with a locally accepted community plan.	<u>Federal performance requirements include housing quality, fair access for protected classes of households, rent reasonableness, and accuracy of income eligibility and tenant payment determinations.</u> Financial penalties for failure to achieve standards. HUD can fund an alternative administrator (high performing LHA) if continued failure to meet standards. Bonus for LHA that meet and exceed performance standards. HUD can waive requirements for localities, consortia, or States that submit innovative proposals for alternative mechanisms to satisfy HUD's performance standards. LHA can make local decision to adjust gross income and rent payment standards but <u>must serve at least 90% of the number for which HUD bases its funding allocation. No more than 10% of recipients pay above 35% of income for rent</u>.
<u>Local performance goals</u> shall also be designed by each agency to measure program performance. They should address; meeting agency plans and goals, housing quality in the program, and community/jurisdictional mobility goals.	High performing LHAs will receive bonus funds up to 15% of incremental and recaptured turnover funds or 1.5% of funds allocated for the total HCF program.

NAHRO Tenant-Based Rental Assistance Program (TBRA) Program - Comparison 5

NAHRO PROPOSAL	HUD BLUEPRINT
<u>Sanctions for nonperformance would result in funding being reduced or eliminated</u>, or an option of allowing another LHA to administer the program.	Financial penalties for failure to achieve standards.
Funding will be distributed to LHAs, by a block grant and will be based on national criteria such as relative unmet need; resident incomes, housing quality, meeting National and local performance standards; and consideration of mobility patterns. The formula will take into consideration the unique needs of agencies operating in both metropolitan and nonmetropolitan areas.	<u>HUD will annually recapture a portion of turnovers and allocate to localities</u> along with incremental by a formula that reflects eligible population with severe need for assistance as defined by recent Census data.
LHAs will be compensated for reasonable TBRA program administrative costs subject to a budget and limited to actual expenses up to a maximum of 15% of the total grant received.	Administrative fees system using low- and high-cost housing markets and in different types of service delivery areas, including geographically dispersed non-metro areas. Fees adjusted annually by a wage index rather than a rent index. LHA will not be permitted to perform inspections or do rent determinations on their own units, local jurisdiction responsible, paid with separate funding.
Each LHA will develop a TBRA transition plan within one year and fully implement their plan within 2-5 years. Transition will most likely occur as contracts are renewed.	

NAHRO's AFFORDABLE HOUSING PROGRAM: A COMPARISON
March 30, 1995

ELEMENTS	NAHRO PROPOSAL	HUD PROPOSAL
Replace existing housing production programs with a single blockgrant, with selected activities permitted.	Yes, block grant would include: - HOME, 202, 811, - National Homeownership Fund, - Housing Counseling, - HOPE 2 & 3, - Lead-Based Paint Hazard Reduction - Selected McKinney programs - Housing for persons with AIDS - Supportive services for special projects up to a 15% ceiling. - No tenant-based rental assistance. - Loan Guarantees	Yes, block grant would include: - HOME, 202, 811, - National Homeownership Fund, - Housing Counseling, - HOPE 2 & 3, - Lead-Based Paint Hazard Reduction - McKinney programs would stay in a separate block grant, to be folded in at future date. - Housing Opportunities for people with AIDS would remain a separate program to be folded in at future date. - Supportive services - Service coordinators for 202 projects - Tenant based rental assistance - Project based rental assistance - Public Housing Mod. - Loan Guarantees

Affordable Housing Program: Comparison

ELEMENTS	NAHRO PROPOSAL	HUD PROPOSAL
Consolidated Plan	Consolidated Plan will be required to identify needs, and set community priorities.	Consolidated Plan required to set priorities for the Affordable Housing Fund, Consolidated Plan, plus new Homeless Plan and a separate Homeless Board, for the Homeless Assistance Fund.
Block grant distributed by formula	New formula allocation based on selected factors of need, with new consideration of threshold for direct receipt of funds.	HUD would use the HOME Program criteria and distribution formula. Separate Homeless Assistance Fund distributed by ESG formula, with "hold harmless" for those who received grants in FY93 or later to remain direct recipients. Also, formula allocation will be average of what was received from FY87 through FY93.
Local/State Split	70/30 local-state split	60/40 local-state split for Affordable Housing Fund 75/25 split for Homeless Block Grant

Affordable Housing Program: Comparison

ELEMENTS	NAHRO PROPOSAL	HUD PROPOSAL
Performance Measures	Requires locally developed performance measures. No withholding of money for performance pool	Requires locally developed performance measures within federally mandated categories Withholds 10% of allocation for performance pool
Population Served	Only restriction would be 100% below 80%.	HOME program mandate of 100% below 80%, and 90% below 60% in rental housing, with 20% of units going to persons below 50% of median. Will permit "a limited portion" of funds to be used for families up to 115% of median in designated low-income areas.
Local Match	No requirement of a local match, statutory language encouraging leveraging of private and non-federal dollars.	HUD is considering either the 25% match currently used in HOME, or a 10% straight cash match. Match requirement would be program wide, not project by project.

3

Affordable Housing Program: Comparison

ELEMENTS	NAHRO PROPOSAL	HUD PROPOSAL
Regulatory Reform	Limited statutory and regulatory restrictions. A few national goals and objectives to guide development of local plan. Adopt relevant elements of NAHRO's CDBG Regulatory Reform proposals.	Maintains the HOME Program regulatory restrictions, including multiple restrictions on rents and income targets, and population served by activities.
Earmarks and Setasides	NAHRO would not have any federally mandated setasides, permitting each recipient jurisdiction to identify their own priorities and select appropriate subrecipients. NAHRO's proposal would restrict the amount that could be spent on supportive services to no more than 15% of program budget.	Up to 30% of funding setaside locally for nonprofits, including LHAs, with 15% going to CHDO's. This would be "benchmark" jurisdiction could request waiver from if can prove cause. New mandate of 10% for Colonias Setasides for states on Mexican border New $16.5 million setaside for HUD Management Information System. $83 million setaside for technical assistance and community viability, $10 million of this to universities.

4

CDBG -- COMMUNITY OPPORTUNITY FUND: A COMPARISON

March 30, 1995

ELEMENTS	NAHRO	HUD
Programs and activities to be included	CDBG Section 108 Loan Guarantee Section 107 Special Purpose Grants Ease of regulation to improve use for economic development, and brownfield redevelopment	CDBG Section 108 Loan Guarantee Section 107 Special Purpose Grants A new job creation Performance Bonus pool for good performers Emphasis on job creation, brownfield redevelopment, and jobs for people on welfare
Consolidated Plan	Consolidated Plan outlines needs, sets community priorities, locally developed performance measures	Consolidated Plan outlines needs, sets community priorities, locally developed performance measures within Federally established categories.
Earmarks and Setasides	No new setasides beyond current special purpose grants at their current funded levels.	Maintain existing special purpose grants, including Colonias setaside of 10% for border states. Increase setaside for Technical assistance and Universities to $23 million. Add new setaside of $18 million for Management Information System.

ELEMENTS	NAHRO	HUD
Regulatory Reform	Maximum regulatory reform and statutory changes will be sought to improve local flexibility and reduce administrative burden.	Few regulatory or statutory changes will be sought, continuing many of the existing regulatory and administrative burdens.
-- **Davis-Bacon.**	Modify Davis-Bacon to improve administrative ease, including an increase in the threshold and reduction in paperwork requirements.	Silent on Davis-Bacon.
-- **Lead-Based Paint.**	Simplify regulations and permit flexible implementation for more innovative solutions and remediation to level of future use.	Maintain current level of regulation, permit lead based paint abatement under Affordable Housing Fund.
-- **Site and Neighborhood Standards.**	Maintain principle of deconcentration as a goal for the program, but permit each jurisdiction to address within consolidated plan.	Silent.
-- **Section 3.**	While supporting the intent of this regulation, NAHRO believes implementation should be locally designed, not a mandated quota.	No change from recent regulatory change that mandates an annual quota for each grantee.
-- **Environmental Review Regulations.**	Reduce unnecessary requirements, permit more local flexibility in deciding how to implement, update regulations to current standards.	Silent.

CDBG--Community Opportunity Fund: A Comparison

ELEMENTS	NAHRO	HUD
-- Uniform Relocation Act.	Remove as a mandate, keep as a principle and as element to be addressed within consolidated plan process on a project by project basis when a project to be federally funded may cause displacement.	Silent. No change from existing regulation requiring grantee to find all tenant that had lived at property up to one year prior, even if they had moved of their own accord.
-- One-for-One Replacement.	Remove as a mandate, keep as a principle and as element to be addressed within consolidated plan on a case by case basis. If a project will require demolition of a unit community should consider and address within plan the need for replacement. Recognize that not every community needs to replace all units.	Silent. No change from existing regulation that every community must fulfill one-for-one replacement requirement.
-- Fair Housing Plan and Affirmatively Furthering Fair Housing.	Support Fair Housing Law, and maintain AFFH as a program goal and eligible activity, but do not require separate fair housing plan from what is already required under Consolidated Plan. Permit fair housing activities outside of the planning/administrative or public services cap.	Permit fair housing activities outside of the planning/administrative or public services cap.

3

CDBG--Community Opportunity Fund: A Comparison

ELEMENTS	NAHRO	HUD
-- Sub-Grantee Monitoring. - Monitoring Agency - Monitoring Plan	When a project is supported by more than one CDBG funder (ie., city and county), permit one funder to do monitoring, sharing their monitoring reports with other funders. Permit grantees to develop modified sub-recipient monitoring plans based upon the level of experience of recipient and complexity of project.	Silent, no change to subgrantee monitoring.
-- State CDBG Program.	Federal government should ensure that state CDBG programs do not become overly burdened with an additional layer of regulation. State CDBG program should be modified to enhance compatibility with Section 108 Loan Guarantees.	Would permit states to carry out activities themselves in nonentitled areas.
-- CDBG Slum-blight.	Permit grantees to use state or locally established definitions which utilize indicators other than existing physical decay, to permit remedies to be enacted at an earlier state.	No change from existing regulation that requires evidence of physical decay, requires slum-blight to already exist, before permitting use of CDBG for slum-blight prevention.

PREPARED STATEMENT OF AUDLEY EVANS

EXECUTIVE DIRECTOR, TAMPA HOUSING AUTHORITY, FL

APRIL 27, 1995

Mr. Chairman, Senator Connie Mack, and Members of the Senate Subcommittee on Housing Opportunity and Community Development, I am honored to have the opportunity to speak before you today. As Executive Director of the Tampa Housing Authority, I take great pride in espousing to you my thoughts on some of the many changes that face our public housing authorities, the communities, and the residents we serve. Based on my experience in Tampa and recently in New Orleans (on special assignment), I have first-hand knowledge of the impact of these changes. Through much effort, our agency in Tampa was lifted from a troubled status to HUD's classification as a Recognized Performer, in FYE 3/31/94 and again in FYE 3/31/95. We are all aware of the problems that have faced public housing communities through the years . . . the deterioration of structures, high density of low-income families in a small geographic area, the promotion of mediocrity, and the countless other social problems resulting from perceptions of life in public housing. The generous welfare system of our great country has in many ways created an adverse reality among our poor:

- Public housing denies residents the right to choose where they live.
- Federal Laws have concentrated the very poor in public housing.
- Local officials have cited public housing developments in high poverty areas.
- Federal Laws penalize public housing residents who work.
- The discipline of the real estate market does not apply to public housing.

In light of the many problems that have faced the public housing industry over the past 50 plus years, the proposed HUD Blueprint offers concrete solutions to some critical issues and for that, I support the efforts of HUD in this Blueprint. The plan proposes to give the direct benefit to the resident rather than the agency or governmental unit. This will give the resident choice of where to call home, thus creating a sense of freedom rather than the feeling of entrapment. Creating choice will force PHA's to improve and maintain the quality of the housing stock in their communities making it competitive with the private market units now available. PHA's can operate like a real estate management organization as they were designed not to be the social service agency they have become. Under the Blueprint, a PHA will enter a transition phase where it will evaluate their stock in the first year, demolish those units that are not economically or otherwise fit to retain, and place the remaining units in a 3, 5, or 6 year transition. PHA's will then be expected to be accountable and proactive in providing the most efficient and effective ways of providing affordable housing in their communities. It is important that PHA's get the assistance and cooperation needed from HUD to insure a smooth and effective conversion. Such critical items include but are not limited to:

- Full modernization subsidy through the transition phase to enable PHA's to bring deficiencies up to competitive standards.
- Full operating subsidy through the conversion phase to enable PHA's to maintain the quality of the stock they wish to preserve.
- Swift approval on creative plans to provide alternative ways of providing affordable housing to the community.
- Full cooperation and ability to demolish those units they deem necessary.
- Changes to the rent rules to enable full ability to properly mix low- and moderate-income families to provide a desirable economic mix in one community and to provide the necessary income to make the project financially feasible. This will include the allowance to charge a fair market rent on the housing stock thus allow PHA's to plan based on a property's potential earnings and become competitive with surrounding private rental communities.
- PHA's must be free to obtain any financing necessary to accomplish their goals.
- Tenant-based subsidy must go to the Housing Authority for administration (as is done in our current Section 8 Programs). The PHA can continue to administer the assistance even if the assisted family moves from the PHA's stock into another assisted unit.

If the transition plan is properly established, it is possible and the availability of affordable housing can be preserved.

The Federal level of Government should set broad policy as it relates to affordable housing, but local governments should have the flexibility to set focused policy applicable to the needs in their individual communities. This flexibility should be allowed with limited intervention from the State level. HUD should ultimately be a regulatory oversight body and not get involved in programmatic issues. It is nec-

essary for Housing Authorities to have the freedom to run their agencies as they see fit without the micromanagement that is often practiced today. After a PHA has developed an organizational structure and guidelines, HUD should review and approve the PHA's plan and develop a review process. The PHA's goals should tie into the city's CHAS. The State level should not intervene in the affordable housing process. Involvement would create an unnecessary level of bureaucracy. The PHA should revisit its cooperative agreement with the city so that a focus is set on cooperation to achieve common goals. This will involve the city offering financial and technical assistance when feasible.

As the pioneer of Tampa's Resident Enterprise Assistance Program (affectionately called Project REAP), I am proud of its now national acclaim and encourage the promotion of the concept of Section 3 of the Housing & Community Development Act. Project REAP provides business training and assistance in an incubator-type environment thus spawning small businesses owned by residents of public housing. I promote and support the microenterprise concept using public housing residents whenever and wherever possible in the operation and modernization of public housing communities. I have said many times that "A hand up is far better than a hand out." The microenterprise concept provides opportunities for choice and financial freedom to many residents with entrepreneurial capabilities. This concept also provides needed training and jobs to others who may otherwise never have the opportunity within their reach. It is time that we concentrate our efforts on providing opportunities for residents to move up and out of public housing if that is their desire. Many residents may never get the opportunity for trade training due to the limitations imposed by the Davis-Bacon Act. Changes to this act are necessary to enable the hiring of residents while they develop the needed skills which command higher wages in the future. At present, Davis-Bacon (and the restraints imposed), discourages the hiring of residents whose current capacity is a training status. If trainees were allowed to be hired at the lower wages their current skills command, it will prepare them for higher future aspirations.

As a result of aggressive economic development programs, the Tampa Housing Authority now enjoys a vacancy rate of less than 1 percent (calculated based on units available for occupancy), consistently greater than a 90 percent collection rate, vacant unit turnaround less than 20 days, faster work order response time, and an overall improvement in the sense of pride among residents. (These statistics are based on FYE 3/31/95 figures.)

The concept of microenterprise promotes the upward mobility of many public housing residents which has a positive impact on the resident, the PHA and the community-at-large. Economic opportunities can lead to the experience of the American dream of home ownership. In Tampa (in partnership with the city utilizing its Challenge Fund and CDBG funds), we have successfully provided affordable home ownership opportunities for more than 100 public housing families. Such concepts can be expanded to enable PHA's to target suitable units in their stock to provide further home ownership opportunities. The proceeds from such sales can be used to provide additional units needed for the PHA's rental program.

This country was founded on the concept of freedom. Freedom to choose . . . freedom to improve the quality of one's life . . . freedom to make the decisions that can impact one's family. I believe we all agree that some form of change in the way we currently provide affordable housing to our needy communities is necessary. There is a real feeling of hopelessness, despair, and lack of self-esteem among many public housing residents. Such continued feelings can lead to drug abuse, crime, and family problems which affect our housing stock and all citizens in a community as well. I look at the changes that currently have a potential direct and significant impact on our country's poor with excitement. With appropriate planning, cooperation, and full HUD support, I view this change as a challenge and welcome the opportunity to be creative as we develop new strategies to provide affordable housing to the needy families in our communities.

Thank you.

PREPARED STATEMENT OF REVEREND WILLIE F. CARTER

EXECUTIVE DIRECTOR, HUNTER'S VIEW RESIDENT MANAGEMENT CORPORATION

SAN FRANCISCO, CA

APRIL 27, 1995

As both political parties agree that public housing is not functioning as intended and must be drastically changed if it is going to survive—one needs only to look

to public housing residents for solutions. Residents across the country have successfully broken public housing monopolies by organizing resident management corporations which provide competitive bids for necessary services such as rent collection, landscaping, maintenance, and property rehabilitation. Residents have proven, time and time again, that they can provide better services at a lesser cost because they have a stake in doing so. Residents and their families must live with the consequences of their actions.

Resident control and ownership are the keys to transforming problematic public housing developments into viable low-income communities. Resident Management provides employment and entrepreneurial opportunities to a population largely excluded by the private sector; a fact which takes on even greater significance as welfare reform is legislated into practice. To court welfare reform without providing avenues of opportunity to the affected population is to court disaster.

Hunter's View Resident Management Corporation

In San Francisco, the Hunter's View Resident Management Corporation (HVRMC) has helped develop a community that I believe exemplifies reform. In 1 year the HVRMC, with funding redirected from the San Francisco Housing Authority, and with technical assistance from the Institute for Contemporary Studies, other community-based organizations, and a very efficient and dedicated staff and paid consultants, our organization has literally changed the structure of our community.

We have initiated and implemented ventures such as our Family Drug and Alcohol Rehabilitation Facility, completely operated by our residents. This program provides families with 12 months of residential substance abuse treatment, counseling, and educational life skills, such as parenting classes, computer literacy training, CPR/First Aid training, and Job Readiness Training. The facility provides a clean environment in which the whole family can heal, and become reacquainted with society and God. The program employs 5 residents full-time.

Our Vacant Unit Patrol venture employs 13 residents to secure housing authority apartments that are waiting to be re-occupied. This program deters would-be vandals from breaking into units to do damage to the property. The Patrol's nightly presence also deters would-be car thieves who would steal our cars, or deposit cars that they have stolen from others on our property. The Vacant Unit Patrol has saved the San Francisco Housing Authority significant operating funds, while also serving to enhance the quality of life in our community.

Our Landscape Company is run by the RMC and employs 20 residents who have received on-the-job training in all phases of landscaping. Our development had been terribly neglected for many years by the Housing Authority so the opportunities for on-the-job training were boundless. Our crew is now experienced in irrigation systems, tree surgery, landscape design, plant arrangement, and all phases of horticulture, including soil composition.

Our RMC operates a laundromat that employs a resident full-time. Unlike other Housing Authority laundromats, we have no vandalism in our resident-run enterprise.

Our RMC management operations are run by 5 full-time resident employees, a resident bookkeeper, and a housing management specialist. The RMC also contracts with a legal firm, 2 certified public accounting firms, and a payroll service.

Other community-based programs include an After School Garden Internship which employs 12 youth to do gardening 2 hours a day during school season and 5 hours a day during summer vacation. A professional tutorial service employs 3 resident-parents as teachers 3 days a week. Our Life Enhancement Program serves up to 60 children a day in combination with the tutorial program and employs 4 resident-teachers. The tutorials focus on bridging the gaps within our declining education system between the parent, the community, and the child. The Life Enhancement Program focuses on non-traditional subjects such as conflict resolution, cultural awareness, leadership development skills/traits, home economics, financial awareness, and responsibility.

Resident Management must be preserved in the housing and welfare reform you are contemplating—if this reform is to truly benefit the 3 million residents of America's public housing. The resident management movement has already addressed the major concern of welfare reform: Creating jobs before terminating benefits. Ninety-five percent of the people now employed by the HVRMC were once recipients of some sort of public assistance. Children who witnessed their parent receiving a welfare check now see them proudly walking to work each day. Twenty percent were drug users or pushers who have now transformed their lives and have become productive members of our beloved community. Crime and drugs were once fixtures at Hunter's View. Now Hunter's View is a place of serenity, peace, and prosperity because community needs have been addressed by our self-reliant residents. To be suc-

cessful at reform we cannot simply address individual behaviors and expect change. We must change the economic structure of the community.

Over many decades, the Government has failed to do what we have managed to accomplish in a year's time with a simple redirection of funding from the public housing bureaucracy to the residents of our community.

Hud Reinvention: *From Blueprint to Action*

HUD's Reinvention Blueprint proposes to consolidate the management of the 60 existing HUD programs into 3 programs. I assume that this change reflects HUD's Mission Statement:

"HUD was created to carry out the Nation's commitment to work for healthy growth in cities, adequate housing for all, and protection of society's most vulnerable people."

While I want to support a consolidated view for the betterment of all people, I am puzzled as to who is referred to as "most vulnerable." One could easily draw the conclusion that the "most vulnerable" people are the poor and low-income families of this great Nation from whose sweat America built its fortune. On the other hand, many might draw the conclusion that the "most vulnerable people" are those who are now faced with the dilemma of having to deal with the results of years of terrible neglect of the plight of our Nation's underclass, compounded by misdirected social policy and programs which have existed mainly to benefit poverty industry bureaucrats. This situation has been exacerbated in every neighborhood by drug distribution, the AIDS crisis, and the moral let-down of our Nation. I question today if this Reinvention effort is anything more than an attempt to justify and expand the cruel injustice that has been inflicted upon a deprived people: America's minorities, Blacks and Hispanics especially. Can 60 years of mismanagement and disdain suddenly come to a halt in 3 years? I do not think so.

The Reinvention Blueprint proposes to channel responsibility down to the local level. This still spells mismanagement: The only difference is that you can more easily hound the crooks at the local level, even though inefficient local bureaucracies will remain inefficient.

Another area in the Blueprint that signals mistrust is the great emphasis placed on de-concentrating large segments of a population—where the concentration is mostly people of color. Residents across this Nation are terrified at the thought of being displaced from their communities, even if those communities are currently plagued with horrible conditions such as drugs, violence, crimes, joblessness, single-parent homes and welfare dependency. Yet, conditions do not have to be this way, as we have demonstrated at Hunter's View.

The Blueprint finds its strength in its aggressive language to promote home ownership, but language supporting *public housing* home ownership is sorely lacking. Home ownership allows residents of public housing to share in the most common vision enjoyed by most Americans: To own their homes. If privatization in some form is the major thrust of this plan, then privatization must begin with the resident organizations that are ready to move forward to home ownership and then be extended to the private sector.

Vouchers ignore the community-based approach to social policy reform. I fear that the voucher system will create an incredible demand for housing, raising the demand far above the supply and causing rents to sky-rocket across America. Noncompetitive public housing stock will be demolished, but there are no provisions for replacement development funds. If voucher holders are unable to find a landlord willing to rent to them, where will they turn? HUD's Fair Housing office?

Rethinking Future Policy

In some of America's public housing developments, over 80 percent of the residents depend on government subsidies for their only source of income. It is possible that a child in these developments will not know even one adult that must get up and go to work in the morning. Crime and drugs are permanent fixtures. Drug dealers are by far the most successful individuals in the area. Solutions to these situations must be community-based, and must be based in economics. Private sector jobs do not exist for all of the people currently on Government assistance; to attain true reform, we must be given the freedom and the tools to create our *own* jobs in our *own* communities.

HOME OWNERSHIP OPPORTUNITIES: There is no incentive for resident management without home ownership. Even though all RMC's may not develop the capacity for total self-governance, without the possibility of the transfer of property, volunteerism contains little incentive. There will never be enough Federal money to rehabilitate all of our public housing. Home ownership allows housing authorities to divest

themselves of unmarketable properties, while giving residents a stake in their own communities.

Over the past 3 years, 133 approveable plans to convert 6,757 public housing units to home ownership have been reviewed by HUD. The plans were submitted by local housing authorities and resident organizations similar to ours. A key statutory requirement for the sale of public housing includes the provision of replacement housing. The impact of the proposed rescissions of new development and Section 8 funds from the Fiscal Year 1995 budget, which will come before you when you reconvene, and the failure to appropriate additional funds to meet replacement housing needs in Fiscal Year 1996, must be re-visited. A firm commitment for one-for-one replacement housing must be obtained prior to the title transfer of a public housing unit. Thus, the delay or unavailability of replacement housing may endanger the actual sale or transfer of the unit despite the extensive work, counseling and training, financing arrangements, and resident home buyer expectations that takes place during the implementation of an approved sales plan.

While there are several options for meeting the replacement housing requirement, the most popular alternative for housing authorities has been building new public housing. The second most requested alternative has been creating additional Section 8 certificates, or vouchers. Congress is now threatening to rescind both of these options. The rescission of new development and Section 8 funds from the FY 1995 budget, and failure to appropriate additional funds to meet replacement housing needs in FY 1996, will have a disastrous impact on approved and approvable public housing home ownership plans for thousands of low-income families across the country.

Additionally, the vouchers you are proposing should be available for use as downpayments and mortgage payments for resident management groups such as ours who wish to preserve our communities by purchasing our developments. The vouchers should be project-based.

Finally, the authority to purchase should rest with the development's residents, not with the local housing authority or HUD.

CEILING RENTS: Rents in public housing have been calculated at approximately 30 percent of income since 1970. Prior to 1970, fair market values determined rents, based on apartment size. The result has been a disincentive to seek employment, the break-up of families, and a concentration of AFDC recipients in family developments. Tenants will not seek work if they are effectively taxed for doing so at a 30 percent rate, or if they lose money by working at minimum wage jobs. Ceiling rents, which are presently an optional waiver subject to HUD approval, should become universal policy for all PHA's. Rents should be capped based on apartment size, regardless of how many wage-earners reside in the household. This means that additional wage earners (e.g., adolescents with part-time jobs) will help the family toward self-sufficiency rather than hurt it by increasing the monthly rent payment.

ELIGIBILITY REQUIREMENTS: Public housing should not be rented to minors. Currently, there is no age limit for eligibility. When teenage mothers move into public housing, they lack the skills necessary to take care of their children and their apartments, pick up antisocial habits from their neighbors, and tend to stay in large public housing family developments for the rest of their lives. They seldom have the initiative to finish their education or seek employment, and are not required by AFDC to do either. Worse, they are then responsible for raising a new generation of recipients.

RESIDENT MANAGEMENT: Resident control is cost-effective, and encourages individual and community responsibility leading to economic self-sufficiency. Residents know that they must create their own jobs in today's market, and have demonstrated that they can do so if given the opportunity. One of the most important elements of resident management is the ability of the RMC's to hold residents to higher standards of behavior than public housing authorities can. Unlike PHA's, who find it virtually impossible to evict tenants for anything other than nonpayment of rent, RMC's formulate their own rules, (much like homeowners' associations), and are legally able to enforce them. RMC's, and other community based organizations, are also well-equipped to change the social structures influencing behavior (e.g., our Family Drug and Alcohol Rehabilitation Facility); HUD social grant programs, such as the Drug Elimination Program, would therefore be more successful and cost-effective if they could be ended directly to the resident organizations, rather than the PHA's.

LOCAL FUNDING CONTROL: Local funding decisions should not be controlled from Washington, DC, as they have been for the last 55 years, with the results we all see. Block grants to the States for welfare or housing are a step forward, although they'll probably be misused without an Administration cap. (In all of the debate over welfare reform, no one has talked about the fact that 70 cents of every dollar cur-

rently goes to Administration-instead, they're focusing on the 30 cents that goes to the recipients.) Delivery of services funded by the block grants should also be locally structured with full participation by the affected population. Nonprofits such as HVRMC must be allowed to compete for provision of these services. Programs like resident management must be promoted vigorously not thrown out with the bath water.

DAVIS-BACON EXCLUSION FOR RMC'S: Wages must be determined at the community level. Minority-owned/community-based entrepreneurial activities cannot get started if they are forced to pay prevailing wages (set by unions) on Government contracts. Enterprise zone exemptions from Davis-Bacon should also be proposed. Why should we expect our residents who may currently be welfare recipients to go to work for minimum wage when we are prohibited from paying it ourselves?

Conclusion

Merely to send the authority to reform welfare and public housing back to the State legislatures is to miss a golden opportunity to influence the direction and living structure of that reform—and to accept the unreasonable assumption that States are somehow the repositories of wisdom and virtue in these areas.

We know that welfare as it exists has tremendous incentives for individuals to enter the system of dependency and it has very real incentives not to leave dependency, once they are in the system. One way real reform can be achieved is by creating strong vibrant communities, with residents empowering one another. The economic and political power to make and implement local decisions must be upheld at the national level, if the daily struggle to make a difference in our communities and our children's lives is to be realized.

If this Subcommittee is truly interested in protecting the "most vulnerable," and providing affordable, decent, and safe housing for all, then you must continue the commitment to resident management and support every opportunity for home ownership in public housing. Creating strong and productive people is directly related to the existence of strong and productive communities. Other indicators that this structure is attainable can be seen here in Washington, DC as you travel to Kenilworth-Parkside, or to LeClaire Courts in Chicago, or to Hunter's View in San Francisco. True reform begins at home.

PREPARED STATEMENT OF SHIRLEY DYKSHOORN

DIRECTOR, OFFICE OF INTERGOVERNMENTAL ASSISTANCE, ND

REPRESENTING THE

COUNCIL OF STATE COMMUNITY DEVELOPMENT AGENCIES [NCSHA]

APRIL 27, 1995

Good morning Mr. Chairman and distinguished Members of the Subcommittee. My name is Shirley Dykshoorn, Director of the North Dakota Office of Intergovernmental Assistance. I am here this morning to testify on behalf of the Council of State Community Development Agencies. I am a past President of COSCDA and currently a member of COSCDA's Board of Directors and chair its Community Development Block Grant Committee.

The Council of State Community Development Agencies welcomes the opportunity presented by the 104th Congress to re-examine fundamentally national housing and development policies.

COSCDA members are State executive branch agencies responsible for a variety of housing, community development, and economic development resources, both State and federally funded. We are interested in a broad spectrum of housing and development issues, ranging from homelessness, to job creation, to local public infrastructure. While COSCDA members work most extensively with local governments, we also work with nonprofit organizations and the private business community. Because of the range of resources we administer and the breadth of the problems and delivery systems with which we work, we believe that COSCDA is in a unique position to make observations and recommendations on national housing and development policy.

We present our testimony in three sections. The first section lays out principles we believe are necessary for re-thinking national housing and development policy. The second section outlines our proposals for fundamental change in national housing and development policy. The final section provides our comments on HUD's Blueprint.

While we limit our testimony to issues directly under the jurisdiction of this Subcommittee, I do want to indicate that COSCDA believes that Congress should review housing and development programs and resources across Federal agency lines in order to develop a streamlined, cost effective, and holistic Federal policy on housing and development.

Principles for Creating New National Housing and Development Policies

COSCDA, advocates a set of nine principles for transforming national housing and development policy. Given the many options available, once defending the status quo is put aside, COSCDA believes these principles provide guidance on judging the appropriateness of various proposals for change.

1. The value of housing and community development-related resources depends primarily on the ability of these resources to increase and sustain the self-sufficiency of individuals and families and to provide economic opportunity and a better quality of life to distressed areas and their residents.
2. States must be central players and must be able to work statewide in efforts to reward work, strengthen families, nurture children, reduce dependency, help people build and maintain assets, and improve the quality of life in poorer areas because these objectives often can be met only (1) by using institutions and resources that reach across multiple local jurisdictions, solving problems with an areawide or regional perspective, and (2) through the collaborative use of housing and development-related resources with human investment-related resources, resources over which State governments have primacy.
3. States need flexibility to meet their priority needs. An expansive, supple, and unfettered performance block grant is the best mechanism to deliver Federal housing and development resources. Narrowly focused programs and programs bound by secondary and tertiary objectives and guidelines, no matter how well intended they may be, cannot well address complex problems that usually vary enormously across the country and over time.
4. Housing and development resources across Federal agencies must be consolidated into a minimal number of performance block grants to eliminate duplicative, overlapping, and cross-canceling objectives, requirements, and administrative expenses and to permit States and their partners to tailor resources to meet their varying priorities. The boundaries of these performance block grants should be permeable, permitting some ability to transfer, or "flex," resources among them. They should be complementary and easily used in concert with one another.
5. Allocating resources, setting priorities, and identifying the specific delivery system are decisions that must be deferred to and made by State and local governments, accountable to an electorate, and working in collaboration with resource deliverers, neighborhoods and communities, and intended beneficiaries.
6. The Federal Government must well articulate a broad goal and purpose, must ensure that basic civil rights are protected, and must set a context that holds grantees accountable for the effective and appropriate use of funds. Performance measures that inform legislators and citizens of the effectiveness and impact of the use of resources must be developed cooperatively over time.
7. Federal programs must provide an adequate amount of funds for Administration, including technical assistance, planning, and problem analysis, program monitoring, and assessment. The Federal Government must not divide administrative funds between States and other entities. When this occurs, the administrative funds available are sometimes too low or too high depending on current administrative requirements and the nature of the subrecipient and activities funded. Each State should determine the allocation of administrative resources within its own State.
8. Federal liability for existing investments and debts should not be passed on to the States. The Federal Government should remain responsible for problematic aspects of previously financed, insured, or otherwise assisted projects and should not unilaterally attempt to devolve or share responsibilities for these projects and facilities. State acceptance of these responsibilities, in whole or in part, should be the result of fully voluntary, mutual negotiations.
9. Planning requirements for consolidated programs or block grants must be minimal; should permit States to use or work from their own planning practices and policy-setting strategies; should allow States to set their own priorities based on their own analyses of needs, examination of resources, including resource providers, and their priority values and goals; and provide a framework of accountability to the State's citizens.

These principles underscore COSCDA's belief that housing and community development resources can and should contribute significantly to promoting the self-sufficiency of families and communities. Because the nature of family and community problems, the utility of delivery systems, and the resources available to address

problems vary enormously across the country, States and localities need flexibility in using Federal resources. This flexibility must include two characteristics. First, federally funded programs must be deferential to a large degree in the setting of priorities, the use of funds, and the utilization of delivery systems. Not only is a "one size fits all" approach usually ineffective and inefficient, it is often counter-productive. This deferential flexibility does not toss aside accountability, but it focuses accountability on local decisionmaking processes and on subsequent review and assessment of performance.

Second, Federal programs must not only be adaptable and deferentially flexible, they must also be unconstrained by undue regulations and detail. One of the biggest criticisms that COSCDA members have of current HUD programs is that they are ladened with requirements, with twists, turns, and shackles. To cope, a grantee must become a "Houdini" to escape or solve these requirements and address the fundamental purposes of the program. Too many resources, too much time and effort, are spent on meeting these "underbrush" requirements; it is not too much of an exaggeration to suggest that the major purpose of the program is often lost in the brambled tangle of secondary and tertiary requirements.

Usually, a piece of this underbrush looks innocent and harmless by itself, and may even look and be desirable. However, just as with any bramble or vine, when they amass, they are often impenetrable and force one to focus energies on hacking through the underbrush immediately in front rather than on reaching an important goal visibly ahead. The task before Congress is to determine those few fundamentals that are basic to national policy, and then to remove those requirements that are secondary or tertiary. The appendix to this statement identifies the key underbrush in current HUD programs. COSCDA urges Congress to eliminate this underbrush and prevent its re-occurrence regardless of the direction taken in transforming national housing and development policy.

COSCDA believes that Federal agency regulations usually take detailed statutory micromanagement one step further by adding additional requirements and definitions. Even with broad statutory language, Federal agencies are apt to favor micromanagement, usually hearing, but not listening to input or reactions to their tentative decisions. We are comfortable in believing that Congress will not micromanage resources and are pleased that Congress appears to be ready to ensure that Federal agency regulations are not a back door way to install this micromanagement.

As Congress rewrites national housing and development policy, it should concentrate on this approach: What is *the* fundamental national purpose of the legislation and what are the *one or two priority and necessary* national goals and objectives? What are the *basic* civil rights and citizen protections that should be included in the legislation? What are the activities that *cannot* be undertaken with the funds provided? How will grantees be held *accountable* in mutually agreeable terms for the performance they have undertaken?

We realize that this is a very different way to write legislation and that it is easier to fill legislation with details and micromanagement provisions than to determine the fundamentals. But, to give an example, once legislation specifies what is eligible, as opposed to what is ineligible as a funded activity, regulations get developed to determine what eligible activities are; and because new activities always arise as technology, institutional capacity, problems, priorities, and definitions change, grantees become mired in negotiation and revised bureaucratic regulations to determine whether a specific activity is eligible. In such circumstances, grantees have to prove that what they want to do is indeed an eligible activity, placing the Federal agency in the driver's seat.

Recommendations for Transforming National Housing and Development Policy

COSCDA believes fundamental change must be made in national housing and development policy. Many alternatives are preferable to the status quo. Although COSCDA has not had the time to spell out in detail a specific proposal that we hold as our priority preference, we are able to outline what we believe is the best approach to the changes necessary in national housing and development policy. In proposing this outline we rely heavily on the principles enunciated in the first section of this paper.

In our opinion, any change in the status quo must effect two priority themes. First, programs must be simple; secondary and tertiary objectives must be avoided; there must be no taste of micromanagement; duplication, inconsistencies, cross-cancelling requirements must be avoided; program design cannot be complicated; nice but not necessary tangents and side-bars cannot fetter resources. There are only so many ways this theme can be stated. The priority we attach to this theme leads

us to support an alternative that essentially starts from a blank state. Otherwise, no matter how fastly held the intention, legislation will only work changes on the margin of current law. And regulations may be changed hardly at all.

Second, programs must be expansive and supple; resources must facilitate and not only permit tailoring to address well the problems, priorities, and capacities that vary so enormously across this country and over time. Categorical or narrowly focused programs do not permit the fashioning of holistic responses to the complex and intertwined problems faced by communities and neighborhoods, especially the poorer communities and the families and people that live in them. We have reached the point, both with our experiences and the nature of our housing and community development problems, where stand-alone projects, picket fence-type resources, and myopic visions (a vision disease often caused by narrow and fettered programs) simply will be unsuccessful, ineffective, and meaningless in the long run.

A CONSOLIDATED HOUSING AND COMMUNITY DEVELOPMENT FUND

COSCDA recommends that the Community Development Block Grant, HOME, McKinney homeless, rural housing grant and loan, and rental assistance programs be consolidated into one housing and community development fund. (While we believe special needs housing, like 202 and 811, should be part of this consolidated program, we do not strongly support or oppose its inclusion at this time.) We also recommend that this fund be allocated so that a minimum of 40 percent is allocated to the States and the balance to entitlement localities and that States be able to use their funds statewide.

We further advocate that maximum flexibility be given States and localities in this fund, provided that Congress identifies the fundamental national purpose and the key priority objectives and goals, lays out the basic civil rights protections, and commits to developing mutually agreeable performance standards so that grantees can be monitored and judged not only by Congress but by their citizens and communities. At a minimum, all the activities currently eligible should be eligible under this consolidated fund; but, as noted earlier, we prefer an approach where the *ineligible* activities are identified. States and localities should have maximum freedom to design their own responses to their priority needs and values; use the delivery system most effective and appropriate to the problems being addressed; and use resources in ways that effectively solve the problems and address these issues as they define them.

To a large extent, the families and communities that are eligible and targeted for assistance by one of HUD's (or one of USDA's housing loan and grant programs) current categorical programs are assisted and targeted by all the others. It makes little sense to have HUD (and USDA) develop unconnected, and usually different and often conflicting, guidelines for these singular programs; it makes no sense for grantees or governments to develop multiple and cost-ineffective administrative bureaucracies, applications, and loan and grant requirements; and it makes no sense to force intended beneficiaries to overcome hurdles and jump through hoops to get the kind and extent of assistance they need to improve their lives significantly and for the longer term. It makes no sense for a national appropriations process that covers several related programs to set very similar resource ratios and patterns for all States and entitlement localities when we know that problems and priorities differ. It makes no sense for the Federal Government to mandate specific uses of the funds or the use of specific deliverers when the nature of problems and solutions and the efficacy and availability of the delivery systems vary across the country and over time.

COSCDA does have several preliminary recommendations on the State role in rental assistance, based on our response to an early HUD draft that proposed a State role.

- States should be able to select the most effective local administrators. Legislation should not mandate that States must use only local governments, or only public housing authorities, or only some other entity. Depending on the State, or even on areas within one State, a local government may be the most effective administering agency; and in other cases it may be a public housing authority, or a community based organization, some other nonprofit organization, or another kind of organization.
- States should not be mandated to make payments directly to landlords. Most States would probably opt to have local administrators make the payments. States should have the option to pay landlords directly; they should not be required to do so.
- States should not be required to establish statewide waiting lists. Although some States may choose to create statewide waiting lists, the geographic size and complexity of most States will make this impractical, at least in the short run.

- The State plan for operating rental assistance should be part of the consolidated plan and should not be a separate, freestanding document and process.
- Within very broad guidelines, States should have substantial flexibility in such areas (this list is illustrative, not exhaustive) as waiting list preferences (the current waiting lists and selection preferences should be discarded), fair market rent determinations, portability, sub-allocation of certificates, income targeting, and minimum housing conditions/codes.

PUBLIC HOUSING

HUD faces an impossible management task in dealing with 3,400 public housing authorities. Although COSCDA agrees that the concept of "vouchering" out public housing should be a viable option in dealing with public housing issues, we do not see it as the universal solution, nor necessarily as even the primary solution. Consequently, our recommendation is that States be given the option of taking overall policy management responsibility for "balance of State" public housing. This recommendation encompasses several major tenets.

First, the option is a State option. A State can choose to become involved or not. There would be no implication that States must or should take on such a role, and if a State declines, it should feel no compunction about declining a role. COSCDA believes that a number of States would initially decide to take on such a role, especially if the role meets the tenets that follow. Over time, we believe that many States would opt for such a role.

Second, States would control the resources that otherwise would flow directly from HUD to individual PHA's. States would have the ability to choose how to provide these resources to individual PHA's: As grants for a variety of management, operation, and capital Improvement activities, including construction as well as demolition; as project-based rental assistance; or as tenant-based rental assistance.

Third, States would be able to negotiate different options with different PHA's and even different options for specific projects within a single PHA. Additionally, States would be able to change strategies over time as conditions and circumstances changed.

Fourth, States should have the ability to effect various kinds of mergers and consolidations among PHA's, including termination of PHA's. Many balance of State PMA's are very small (tiny would be an apt description) and may be cost-ineffective.

Fifth, a State's approach to implementing a PHA role, if a State chooses this option, should be included in its consolidated plan (or successor) process and document.

COSCDA believes that in the long run this recommendation would accomplish two very important objectives. First, it would begin the process of rationalizing and integrating housing and related assistance throughout much of a State. Second, it permits States to make decisions in concert with PHA's and others about public housing issues—and this is a much better approach than developing a "one size fits all" strategy and having a Federal bureaucracy deal directly with 3,400 public housing authorities.

Comments on HUD's Blueprint

COSCDA, in a very general way, supports the overall direction of HUD's Blueprint in that it generally makes little attempt to defend the status quo. Overall, we think the general directions laid out in the Blueprint—in program consolidations and performance funds, in re-thinking public housing and rental assistance, in dealing very differently with older project-based subsidies, and developing a new role and stance for the FHA—are largely correct. *However, while COSCDA believes the Blueprint is better than the status quo, we do not believe it is the best alternative to transforming national housing and development policy. Further, even with the changes we propose in the following section, COSCDA believes that the Blueprint is not the preferred alternative for changing national housing and development policy.*

COSCDA comments on HUD's Blueprint for two reasons. First, if Congress uses the Blueprint in whole or in part, we want you to know what we like and dislike about it and how we would change it to make it a more appropriate vehicle for transforming national housing and development policy. Second, the Blueprint is the only fully developed position of a systemic proposed change in national housing and development policy now available. For that reason alone it should be seriously reviewed and critiqued.

We divide our response to HUD's Blueprint into three areas: Community planning and development, rental assistance, and project-based subsidies, including public housing. Our comments on the Blueprint are based on HUD's March transmittal to Congress; we have not yet seen HUD's proposed legislative language.

COMMUNITY PLANNING AND DEVELOPMENT (CPD)

To the year 2000, HUD proposes three consolidated programs in CPD: The Community Opportunity Fund, the Affordable Housing Fund, and the Homelessness Assistance Fund. While we believe that HUD's recommendations improve current law, we disagree in several areas and recommend changes in HUD's proposals, although this is not to suggest that even with these recommended changes, HUD's Blueprint represents the best of alternatives.

Community Opportunity Fund (COF)

COSCDA supports using the CDBG program as the base of the proposed COF. If Congress moves in this direction, it should eliminate, as stand-alone authorizations, the programs comprising the COF.

- COSCDA strongly supports HUD's proposal to permit *States* to carry out activities in non-entitled areas. While most States will continue to use local governments as the dominant provider of programs and projects funded through COF, the nature of some problems or solutions and the varying capacity of delivery systems, including localities, sometimes clearly warrants using another provider of programs or projects funded through COF. We believe States should possess the option of using the delivery system that best addresses the problems.

Although HUD's Blueprint suggests substantial flexibility in uses of COF funds, COSCDA encourages Congress to consider making loan loss reserves (guarantees) and bonding guarantees eligible activities. These may be spelled out in the legislation that HUD has drafted for the Blueprint, but COSCDA has not yet seen this legislation. Loan loss reserves can be a cost effective way of producing housing and development investments and bonding guarantees can be a very effective way to promote minority business development.

- Unfortunately, HUD's delineation of COF makes it appear as if HUD wants to keep nearly all its categorical program structure. For COF to be valuable to States and localities, COF resources must be used to meet local priorities within the context of national goals. Yet, HUD's proposed performance bonus structure appears to be a strategy to keep a centralized, top-down set of categorical programs, such as the Economic Development initiative and empowerment zones, as well as community viability and LIFT, which are programs that Congress did not authorize last year. Limiting the performance bonus pool to larger-scale economic development projects not only lets these categorical programs arise phoenix-like after the birth of the COF "consolidation" but may force States and localities to pursue more economic development than they otherwise would in order to access part of the bonus pool.

- COSCDA supports the notion of performance funds, but we believe that in programs that provide funds through a formula allocation, that grantees should NOT immediately have a certain percentage of these funds withheld in order to provide them subsequently to good performers. This is akin to starting off by saying that all grantees are bad performers until they prove otherwise and that a Federal bureaucracy will withhold funds all grantees would otherwise get until they prove otherwise. COSCDA believes that all funds should be allocated and that any performance bonus pool should be comprised of funds taken from poor performers. This gives all grantees a fair chance to use all their funds and does not penalize everyone by withholding funds up-front.

A second concern that COSCDA has with HUD's proposed performance fund is the difficulty of developing performance measures, especially "outcome" performance measures, in housing and development. Rarely are performance measures developed, used, and applied to housing and development. This is largely because performance measures in these areas are not easily created, even conceptually.

While HUD's Blueprint says the consolidated plan will identify the measures against which a grantee's performance will be judged, there is enough elsewhere in the Blueprint to suggest that this is another area where HUD wants to maintain top down control. COSCDA supports the notion of performance measures and believes that performance measures must be developed primarily from the ground up. Doing this requires honest collaboration and takes time. HUD cannot simply "establish national goals and objectives" and then mandate that grantees determine how to achieve these goals. States and localities must be thoroughly involved in the discussion of the "categories" that form the basis of performance and cannot and should not simply receive these categories from HUD.

Finally, COSCDA believes that a grantee's use of a performance bonus pool should not be limited to types of activities selected by HUD or that HUD should pre-approve activities financed by access to the bonus pool. Access to a performance bonus pool should be accomplished by performing well in meeting your own priorities with-

in the context of broad national objectives, and funds from the bonus pool should be used to meet local, and not HUD, priorities.

• HUD's COF proposal also contains mandatory setasides. While COSCDA does not object per se to the purposes of these setasides, we believe that most should be specifically earmarked at a specific dollar level rather than as a percent of the COF appropriation. This would ensure that an appropriate sum will be available for these purposes and that these activities would have to be approved annually by Congress rather than being on automatic pilot. For example, COSCDA believes that HUD needs to improve its management information systems, but these funds should be specifically appropriated and approved each year by Congress; HUD certainly should not need large sums of money indefinitely for this purpose.

• COSCDA recommends that administrative fund provisions in the COF not be arbitrarily split between State and local administrative costs. The current CDBG program caps administrative costs at 20 percent of the amount allocated to a State, but then further caps State administrative costs at 2 percent. Although COSCDA believes a 20 percent cap is appropriate if the program is streamlined and the underbrush cleared away, the treatment of administrative costs in the State-managed program should be similar to that in the current HOME program, where each State, working with its localities, determines how to split administrative costs. Further, the current CDBG program requires that States match Federal administrative funds on a one to one basis. This match requirement is more bother than it is worth, and COSCDA recommends that this administrative match requirement be eliminated in the COF. Also, given the importance of the consolidated plan, planning must be an eligible administrative activity. Finally, any program developed by Congress should provide that a grantee can use a limited amount of funds for technical assistance and capacity building.

Affordable Housing Fund

Because COSCDA believes that the most effective housing delivery mechanism is a block grant approach that provides States and local governments the flexibility to address their own specific and very diverse housing needs, we support the concept of the Affordable Housing Fund. We realize that including special needs housing, such as housing for the elderly and the handicapped, is controversial. But States use the HOME program for housing for the elderly and the handicapped and we believe States can handle devolution of housing for the elderly and the handicapped. The consolidated plan process and content (and the Comprehensive Housing Affordability Strategy in prior years) well articulates special needs housing, and it is a type of housing need that States will not overlook. Finally, any housing fund should ensure the promotion of home ownership.

• While conceptually supporting HUD's Affordable Housing Fund, COSCDA does believe that several changes would make the AHF a more effective housing resource. The most significant change we propose is that 100 percent of the funds be allocated to State governments. We realize this is a very controversial recommendation, but we make it for several good reasons.

First, housing markets tend to be regional in geographic scope and often, except in some rural areas, encompass a multitude of localities. States are the only governmental institution with the authority to work across local government boundaries.

Second, COSCDA has long supported the principle that housing must nearly always be linked with human service resources, and we have worked during the past seven years with the American Public Welfare Association to promote housing and human service collaboration. We strongly believe in this principle because we believe that housing funds should largely be used to encourage and sustain self-sufficiency and economic independence for lower-income households. States have always dominantly controlled human service resources, and collaboration between housing and human services can be greatly facilitated if the housing and human service delivery systems are similar to one another.

Third, and perhaps most important, in 1995 Congress will provide substantially more power and flexibility to States in the general areas of welfare and poverty. While the final shape, number, and details remain to be determined, States will completely control several large block grants that consolidate many welfare related programs. In doing so, Congress is assigning States, and States are accepting, the responsibility for ending welfare dependency and making a substantial dent in poverty. Housing must play a critical role in ending welfare dependency and reducing poverty. Most of the more substantial challenges reside in urban areas. Welfare reform nearly requires that States be able to blend housing and a broad swath of human service resources to enable dependent populations to become economically independent and self-sufficient. This extent of collaboration is also necessary to pre-

vent those who are near-poor, especially those who are working, from becoming poor. Thus, housing resources should largely parallel emerging welfare reform initiatives and be largely directed to States.

• Our second recommendation for change in the AHF is to require a "cash" match of 10 percent with eligible matching cash contributions to include: Non-Federal cash or cash equivalent subsidies in affordable housing, State-funded rental assistance programs, private owner-donated cash or cash equivalent investments in affordable housing, bond proceeds, and Federal and/or State funds used to purchase or fund supportive services linked with affordable housing opportunities created through the AHF. We believe there should be a match requirement to secure and maintain the "partnership" arrangement of the HOME program, a partnership that has provided additional subsidy funds for the provision of additional affordable housing opportunities. And we believe our recommendation replaces a complicated match requirement in the HOME program with a simpler requirement. Most importantly, we believe that this match requirement and definition will greatly facilitate the housing and human service collaboration necessary to promote self-sufficiency and economic independence opportunities, especially for people dependent on welfare.

In addition to this basic recommendation on match, COSCDA believes that a full match waiver should be available for States that meet any of the three distress criteria of poverty, per capita income, or personal income growth.

• In regard to income targeting, COSCDA believes that the HOME income targeting now required should be simplified by eliminating the requirement that a HOME-assisted project must have at least 20 percent of its units set aside for households with incomes of less than 50 percent of median income. The current HOME requirement of program-wide targeting—100 percent of the funds serving households at 80 percent or less of median income and 90 percent serving households at 60 percent of the median income—should be maintained.

In nearly any housing program, income targeting should not repeat the mistakes of the past by imposing deep restrictive targets on eligible populations that serve only to segregate the very poor into large housing developments. A more effective housing policy is one that reduces separation by race and income, facilitates the development of mixed-income housing, and provides opportunities for self-sufficiency and economic independence.

• COSCDA recommends that several activities be clearly made eligible activities in the AHF, and this includes tenant-based rental assistance. We also strongly believe that AHF funds should be used for what we call "initial project-based" assistance. In this approach, rental assistance would be project-based only at initiation; rental assistance would be assigned to a specific development based on commitments to lower-income households. But once a tenant has signed the lease, the assistance would become tenant based. This is an effective use of tenant-based assistance as a tool for promoting self-sufficiency, especially when a developer builds housing adjacent to or with easy access to areas where job growth is occurring or provides a range of support services for tenants.

If there is no match requirement that includes Federal and State funds for self-sufficiency activities, then COSCDA recommends that the AHF permit the use of funds for support services integral to the housing being developed and consistent with the objective of self-sufficiency and economic independence.

There are other suggestions we have for eligible activities (relative to the use of program income, debt service reserves, project specific escrow accounts, and an expanded definition of administrative costs), but getting into these details falls into the trap of negotiating with a detailed set of Federal requirements and accepts the status quo as the correct way of doing business.

• In several areas, we make the same or similar comments on the AHF as we did on the COF: Performance bonus, performance measures, and setasides.

• As our comments on the COF indicate, we also believe that the AHF needs to be streamlined more than what HUD suggests in its Blueprint. The appendix to this statement illustrates items that should be eliminated in the AHF.

Homeless Assistance Fund (HAF)

COSCDA has supported a consolidation of the McKinney housing programs since the 1987 enactment of the McKinney Act. COSCDA also supports the "continuum of care" concept. Our recommendations for changes in the AHF include the following.

• We believe it is absolutely vital that States be able to use HAF funds statewide, for many of the reasons identified in our comments on the AHF. Additionally, there are localities that are reluctant to deal with their homelessness problem. For this reason, States should be able to supplement locally administered funds when they

are insufficient. We also recognize that while homelessness is a problem throughout the Nation, in urban and rural areas, it is concentrated in the larger central cities. Consequently, COSCDA recommends that HAF funds be split 50–50 between States and entitlement localities and the States be able to use their funds statewide, as is the case in the current Emergency Shelter Grants program.

• COSCDA recommends that States be able to fund directly both local governments or nonprofit organizations. Often a locality will not apply for homelessness assistance funds even though a homelessness problem exists as do competent homelessness assistance organizations. A local government's decision to avoid dealing with its homelessness problem should not preclude other ways of providing assistance to those in need in such localities.

• We also recommend that there be no cap on using HAF funds for homelessness prevention and essential services. These activities are absolutely essential if a significant dent is going to be made in the homelessness problem. Given the tremendous burden on human service resources, this flexibility is warranted.

• If there is a match requirement in the HAF, COSCDA recommends a 10 percent match that permits States and localities to use their current expenditures for homelessness activities to meet the match requirement.

• COSCDA believes that the HAF does not need to be held out for 4 or 5 years as a program separate from the AHF, and we suggest that the HAF be integrated into the AHF after 2 years.

• *As a more important and general point, COSCDA believes that if Congress develops two or more consolidated funds, e.g., COF, AHF, and HAF, that grantees be able to "flex" an amount of money among them. A national appropriation for two or more related programs develops a single funding ratio among the funds. While this may indeed be appropriate as a national average, it is often inappropriate for any individual grantee.* Thus, Connecticut (and we use these examples for illustrative purposes only) may want to spend, and very appropriately so, more money on homelessness and housing and less on economic development and infrastructure than permitted by national appropriations, while North Carolina may want to spend more money on economic development and infrastructure and less on housing and homelessness.

• Finally, COSCDA makes the same or similar comments on topics like the performance bonus pool, performance measures, and setasides as we make on these topics in our comments on the COF.

HOUSING

Public Housing

COSCDA generally supports the notion of eventually transitioning from financial assistance directly to public housing authorities to tenant-based rental assistance to the occupants of public housing. However, we are not sure that this should apply to each and every housing authority and to each and every public housing development; nor are we sure that this transition can be made according to one or several set schedules and procedures.

COSCDA also believes that HUD has an impossible management assignment in dealing directly with 3,400 public housing authorities (PHA's). With this assignment, HUD is likely to develop a detailed, one size fits all approach to PHA's that is outrageously stultifying and/or a "what you don't see can't hurt you" view that keeps HUD distantly aloof from PHA's.

Rental Assistance

Again, COSCDA supports the general values and themes included in HUD's Blueprint recommendations on rental assistance. We believe, however, that the Blueprint's recommendations regarding rental assistance run into the same kind of management impossibilities noted in our discussion of public housing. Further, the recommendations contained in the Blueprint seem overly detailed and complicated.

Project-based Subsidies

Again, COSCDA supports the general thrust of HUD's recommendations in dealing with the huge problems of previously funded project-based subsidized developments. However, we believe HUD's approach must be undertaken cautiously. Projects with rents higher than market should have these rents reduced; many projects should transition entirely to tenant-based assistance, often with a transition that includes temporary project-based rental assistance; and perhaps some projects should continue to receive project subsidies, although for a limited duration so that these projects can be periodically re-assessed to determine the best long-run solution.

COSCDA believes that many States are ready and interested in working with HUD to solve these problems. However, we are adamant in stating that States and localities should not be saddled with any direct or implied requirement to assist these projects financially.

FHA

Our only comment on the Blueprint's FHA recommendations is that they move in the right direction. Clearly, developing the best solution to the FHA situation must involve all organizations, especially those in the private sector, that are directly affected by or use FHA assistance.

A Concluding Comment

COSCDA's comments on HUD's Blueprint and our recommendations for major policy changes in national housing and community development policy should not be interpreted as saying that all Federal housing and development policies are flawed. Clearly, some are ineffective and a few may actually be adverse in their consequences. We believe that the HOME program, especially due to congressional amendments and HUD's subsequent relaxation of regulatory requirements and specificity, is working well and we have always believed that the CDBG program is one of the most effective Federal programs bar none. We think that a McKinney consolidation has much potential. Nonetheless, we believe the resources for these and other programs can be much more effectively used if these and other programs were consolidated and simplified and further authority and power devolved to State and local governments within the context of fundamental national purposes and objectives, basic civil rights protections, and performance standards. More importantly, however, COSCDA believes that the nature of housing and community problems have become so intense and complex that States and localities need resources from which they can tailor responses to these problems and engage solutions in a collaborative and holistic fashion so that meaningful results for the long term are ensured.

Finally, COSCDA realizes that Congress must and will reduce Federal funding. However, while we accept and support this reality, we do not support consolidation as a means to achieve major budget savings, as a way of "gutting" the Federal presence in housing and development, a presence that must be retained in the appropriate ways. We also understand that outlay savings must be gained from the future way we deal with the housing subsidized in the past. We need both to fix past mistakes and move in new directions to meet new challenges. We urge Congress not to cut necessary programs that work well and can work even better to make the large reductions in budget outlays necessary to pay for mistakes of the past.

Mr. Chairman and Members of the Subcommittee, this concludes our statement. I will be pleased to try to answer any questions you may have or respond to any issues that you may raise. I also want to offer COSCDA's assistance to work with you and your staff to help develop the major characteristics, details, and legislative language necessary to transform fundamentally national housing and development policy. Thank you for the opportunity to put our views and recommendations before the Subcommittee.

Appendix

Since HUD is using the CDBG and HOME programs as the basis for its consolidated performance funds, COSCDA believes Congress needs to devote attention to stripping away the built-up underbrush that, especially when considered in total and not singularly, reduces the efficiency and effectiveness of the core programs. Over time, Congress has gradually added secondary and tertiary objectives to HUD programs that make achieving the fundamental purposes of the programs more difficult. Additionally, different Administrations add to regulations both to respond to statutory changes and to instill their own specific values and objectives. Consequently, regulations become more detailed and extensive, resulting in extensive micromanagement.

COSCDA highlights only some of these issues in what follows.

CDBG

- ENVIRONMENTAL REVIEWS. Federal agencies, including HUD, EPA, USDA, and EDA, must adopt uniform regulations in enforcing the National Environmental Protection Act (NEPA) to facilitate the funding of projects from different Federal programs and prevent duplicative, unwieldy, and unnecessarily costly reviews.
- SECTION 3. Modify Section 3 requirements so that States and grantees certify their efforts to hire as many qualified low- and moderate-income persons as possible. Privately owned construction, partially subsidized by Federal programs, should not be subject to Section 3 requirements.

- DAVIS-BACON WAGE RATES. Eliminate Davis-Bacon wage rate requirements; they increase construction costs by as much as 30 percent in rural non-metropolitan areas and unnecessarily add to the costs of trying to provide benefits to lower-income people.
- HUD REFORM ACT DISCLOSURE. States should be exempt from the disclosure provisions in the HUD Reform Act. Existing regulations, such as those regarding conflict of interest and open and fair procurement processes, already provide for this kind of disclosure.
- PROGRAM INCOME. Program income funds should lose their Federal identity after project close-out so that States and their grantees can make better use of these funds and reduce the amount of State and local staff time and cost to monitor program income compliances.
- SINGLE AUDIT ACT. States should be allowed to determine the audit responsibilities of communities with populations of 2,500 or less. The Single Audit Act, which was designed to reduce the audit responsibilities of localities by permitting them to submit a single audit for all the Federal program funds they receive rather than a single audit for funding for each Federal program, is ill-suited for many rural communities who may receive only HUD CDBG funds.
- ECONOMIC DEVELOPMENT AND JOB CREATION ACTIVITIES. While HUD's recent economic development regulations facilitate the use of CDBG funds for economic development activities, several additional adjustments should be made relating to job quality, infrastructure improvements for economic development purposes, appropriateness testing, lump sum draw downs, and draw down or expenditure definitions.

[NOTE: See the attachment to this appendix for administrative citations for the State-administered CDBG program.]

HOME

- MATCHING REQUIREMENTS. Match from non-HOME affordable housing should not be required to be repaid to the HOME Investment Trust Fund as long as repayment continues to be available for affordable housing.
- MONITORING REQUIREMENTS. Annual on-site reviews of assisted units are a daunting and cumbersome task for States; instead of requiring annual on-site reviews, States should prepare and follow a monitoring plan that meets broad HUD standards.
- HOUSING QUALITY STANDARDS (HQS) AND HOME-ASSISTED HOUSING. While HQS may appear to establish a minimum threshold of quality, it precludes States from using HOME funds for emergency assistance, weatherization, or handicapped accessibility assistance. Additionally, HQS may be overly rigid: For example, if a unit does not have a formally designated "living room," it fails HQS. States should be allowed to use HOME funds to address life-threatening problems or to prevent further deterioration of a unit (e.g., roof repair). COSCDA recommends exempting housing units receiving $5,000 or less in HOME ends for weatherization, emergency assistance, home repair, or handicapped accessibility from HQS requirements. Also, only FHA inspection and standards should apply to home ownership activities, rather than Section 8 HQS inspection and standards. This change would comply with current standards in the private mortgage industry.
- LABOR REQUIREMENTS. Davis-Bacon labor wage rates should not apply to AHF funds.
- ENVIRONMENTAL REVIEW. The current exemption of first-time home buyer and tenant-based assistance programs from environmental review requirements should be expanded to include one- to four-unit rehabilitation.
- EXPENDITURE DEADLINE. The current 15-day time limit is particularly burdensome for States, counties, and consortia that deal with multiple recipients. Moreover, it is problematic with the draw down of administrative funds, resulting in smaller and more frequent disbursement to subrecipients. COSCDA recommends that the 15-day period be lengthened to at least 30 days.
- REHABILITATION ACTIVITIES EXEMPTION. Allow certain kinds of rehabilitation to be provided to homes over 50 years old without clearance by the State Historic Preservation Office. There are at least 24 rehabilitation activities that could be exempt from historic review (e.g., attic and crawl space insulation, caulking and weatherstripping, re-roofing and/or painting with similar materials and colors, installation of kitchens and baths). Currently, none of these activities may be done without historic approval.
- ACQUISITION OF HUD-OWNED PROPERTIES. Allow AHF funds to be used to acquire HUD-owned houses prior to approval by the State Historic Preservation Office or allow CHDO's at least 45 days to purchase HUD-owned houses. HUD will cur-

rently hold a home only 2 weeks for purchase by a nonprofit developer, but historic clearance typically requires at least 30 days.

- SECTION 3. Section 3 requirements should be met through certification (see CDBG recommendation).
- OFF-SITE IMPROVEMENTS. "Site improvements" should be more broadly defined to allow HOME funds to be used for off-site improvements such as streets and sidewalks where the jurisdiction deems such activities necessary.

ESG

- PREVENTION AND ESSENTIAL SERVICES. The 30 percent caps on prevention and essential services should be eliminated. States are finding that utilizing ESG monies to fund prevention saves money in the long run because it alleviates the need for individuals and families to utilize more extensive homelessness services.
- NEW CONSTRUCTION AND ACQUISITION. Currently, acquisition for or construction of shelters are ineligible activities; they should be eligible.
- DEADLINES FOR USING GRANTS. Current ESG regulations require each State to make available its allocation to State recipients within 65 days of its grant award by HUD. It is difficult for some States to review all applications for funding and notify each applicant within 65 days when technical assistance must be provided to help applicants develop competitive applications. Regulations also require States to use their homelessness prevention funds within 180 days. A time limit cannot be placed on homelessness; homelessness prevention funds are needed throughout the year.

Attachment to Appendix

COSCDA

SMALL CITIES CDBG PROGRAM CITATIONS

Administration and Management

Issue	CDBG Citation	Controlling Regulation	Executive Order	Statute
Citizen Participation	570 486	570 486		
Award of Funds (Payments)	570 489(c)	*24 CFR 85.21* 31 CFR 205		
Fiscal controls/accounting procedures	570.489(d)	24 CFR 85.20		
Allowable Costs: Grantee	570 489(a)	24 CFR 85 22		
Non-Profit Subrecipient		OMB Circular A-122		
For-Profit Subrecipient		48 CFR 31		
Program Income	570 489(e)	*24 CFR 85.25*		
Revolving Funds	570 489(f)	570.489(f)		
Procurement	570.489(g)	24 CFR 85.36		
Conflict of Interest	570 489(h)	24 CFR 85 36(b)(3) *24 CFR 570.610*		
Close-out	570 489(i)	24 CFR 85.50		
Property Management	570 489(j)-(k)	24 CFR 85 (31)-(33)		
Debarment and suspension	570 489(l)	24 CFR 85.35 *24 CFR 570 609*	12549	
Audits: of Grantees	570 489(m)	*24 CFR 85.26* 24 CFR 44		Single Audit Act
of Non-Profit Subrecipients		24 CFR 45		Single Audit Act
Recordkeeping	570 490(b)	24 CFR 85 42(a)-(d)		
Access to Records	570 490(c)	24 CFR 85 42(e)		
Monitoring	570 492	24 CFR 85 40		
Sub-grants		24 CFR 85 37(b)		
Enforcement (and Remedies)		24 CFR 85 43		
Termination (for Convenience)		24 CFR 85 44		
Copyrights		24 CFR 85 34		

Environmental Protection

Issue	CDBG Citation	Controlling Regulation	Executive Order	Statute
Environmental Review Procedures	24 CFR 570 604	24 CFR 50 and 58 *40 CFR 1500-1508*	11514 *(a 11991)*	National Environmental Policy Act of 1969
Floodplain Management	24 CFR 50	24 CFR 55 *40 CFR 59-79*	11988	Flood Disaster Protection Act of 1973
Protection of Wetlands	24 CFR 50		11990	

COSCDA

Issue	CDBG Citation	Controlling Regulation	Executive Order	Statute
Minimum Property Standards	24 CFR 50	24 CFR 200		Flood Disaster Protection Act of 1973
Historic Preservation	24 CFR 58.5(a)(1)-(3)	36 CFR 800	11593	National Historic Preservation Act of 1966 Reservoir Salvage Act of 1960, as amended by the Archeological and Historic Preservation Act of 1974
Clean Water				Federal Water Pollution Control Act
Clean Air				Clean Air Act
Coastal Zone Management	24 CFR 58.5(c)			Coastal Zone Management Act of 1972
Sole Source Acquifers	24 CFR 58.5(d)			Safe Drinking Water Act of 1974
Endangered Species	24 CFR 58.5(e)			Endangered Species Act of 1973
Wild and Scenic Rivers	24 CFR 58.5(f)			Wild & Scenic Rivers Act of 1968
Farmlands Protection	24 CFR 58.5(h)			Farmlands Protection Policy Act of 1981
HUD Environmental Standards	24 CFR 58.5(i)	24 CFR 51		

Labor Standards

Minimum (Prevailing) Wages	570.603	29 CFR 1, 7		Davis-Bacon Act
Pay Deductions	570 603	29 CFR 3		Copeland Anti-Kickback Act
Work Hours/Job Safety	570 603	29 CFR 5		Contract Work Hours and Safety Standards Act

Civil Rights, Equal Opportunity, Fair Housing

Non-Discrimination/Civil Rights: Grantee and Subrecipients Contractors	24 CFR 570.601(a)	24 CFR 1 41 CFR 60-1	11246	Title VI, Civil Rights Act of 1964
Equal Employment Opportunity Grantee and Subrecipients Contractors**	24 CFR 570 607(a)	24 CFR 1.4(c)(1) 41 CFR 60-4	11246	Title VI and VII, Civil Rights Act of 1964
Access to Benefits (non-discrimination)	24 CFR 570 602	24 CFR 570 602		Section 109 of Title I, Housing & Community Development Act of 1992, as amended
Age Discrimination	24 CFR 570 602(c)	24 CFR 146		Age Discrimination Act of 1975, as amended
Handicapped non-discrimination Grantee and Subrecipients Contractors	24 CFR 570 602(c)	24 CFR 8 41 CFR 60-741	11914 11758	Sections 503 and 504 of the Rehabilitation Act of 1973, as amended
Disabled/Vietnam Era Veterans Grantee and Subrecipients Contractors		41 CFR 60-250	11758	Section 402 of the Vietnam Era Veterans Readjustment Assistance Act of 1972, as amended

COSC_A

Issue	CDBG Citation	Controlling Regulation	Executive Order	Statute
Employment, Training and Contract Opportunities	24 CFR 570.607(b)	24 CFR 135		Section 3 of the Housing & Urban Development Act of 1968
Small, Women and Minority Owned, and Surplus Labor Area Businesses*		24 CFR85.36(e)(3)		
Fair Housing	570.487(b) 570.601(c)	24 CFR 107 24 CFR Subtitle A	11063	Title VIII of the Civil Rights Act of 1964, as amended Section 104 of the Housing & Community Development Act of 1974, as amended Title VI of the Civil Rights Act of 1964, as amended

* Required of all prime contractors, regardless of dollar amount of contract, if subcontracts are to be let. ** Construction contracts only

Property Acquisition, Displacement and Relocation

Displacement	570.606(a)-(c)	HUD Handbook 1378		Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970
Relocation	570.606(d)	HUD Handbook 1378 *49 CFR 24*		Housing and Community Development Act of 1974 (Section 104(d) of Title I)
Property Acquisition	570.606(e)	HUD Handbook 1378 *49 CFR 24, Subpart B*		URA

Other

Lead-Based Paint	570.487(c) 570.607	24 CFR 35		Lead-Based Paint Poisoning Prevention Act

PREPARED STATEMENT OF JAMES L. LOGUE III

EXECUTIVE DIRECTOR, MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY

ON BEHALF OF THE

NATIONAL COUNCIL OF STATE HOUSING AGENCIES

APRIL 27, 1995

Mr. Chairman, Senator Kerry, and Members of the Subcommittee, thank you for the opportunity to testify this morning on the Administration's plan to reinvent the Department of Housing and Urban Development (HUD) and its programs.

I am Jim Logue, Executive Director of the Michigan State Housing Development Authority and Vice President of the National Council of State Housing Agencies (NCSHA). Under the previous Administration, I served HUD Secretary Jack Kemp as the Department's Deputy Assistant Secretary for Multifamily Housing Programs. I am here this morning on behalf of NCSHA, which represents the housing agencies of the 50 States, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands.

State Housing Finance Agencies (HFA's) have issued more than $100 billion in Mortgage Revenue Bonds (MRB's) to finance nearly 1.6 million lower-income families' home purchases and over $35 billion in bonds to finance over 700,000 rental apartments. NCSHA's member agencies also administer the Low-Income Housing Tax Credit (Tax Credit) program which, since 1987, has helped finance more than 700,000 apartments for low-income families. In 40 States, NCSHA's members administer the HOME program and are responsible for over 70 percent of all State HOME funds—nearly $1.5 billion to date.

Mr. Chairman, State HFA's recognize that Federal budget constraints and HUD's own limitations require this Congress to change the way that Federal housing assistance is delivered. The State HFA's want to work with you to assure that such changes do the least amount of harm to the smallest number of needy families.

We believe that the Congress can and should fundamentally rewrite the Federal Government's housing assistance policy to help those who truly need it while substantially reducing the Federal housing bureaucracy, eliminating duplicative and failed programs, reducing Federal budget costs, and empowering decisionmaking at State and local levels. The Administration's reinvention plan moves in this direction. However, the Administration's plan would leave HUD with more responsibility than it, has capacity, and would severely limit State responsiveness, efficiency, and innovation through unnecessary and burdensome program requirements and funding conditions.

As you re-think Federal housing policy we urge you to:

- Reduce the Federal housing budget by achieving every possible saving from program consolidation, streamlining, and State and local administration, but maintain a Federal investment in affordable housing adequate to sustain at least the present level of Federal effort.
- Give States maximum flexibility through Federal housing block grants to efficiently, effectively, and creatively deliver Federal affordable housing assistance responsive to their unique needs and conditions.
- Assure affordable home ownership and rental housing opportunities for lower income and underserved families and in all markets under all economic conditions by preserving the essential role of the Federal Government in providing mortgage insurance.

Maintain the Present Level of Housing Effort

The amount of funding provided for housing block grants should be adequate to serve at least the number of people presently served by low-income housing assistance. Savings from reducing bureaucracy and simplifying programs must be realistically estimated, not just guessed at. Those savings are not likely to exceed the 10 percent Republican Governors believe can be saved by block granting welfare assistance to the States.

Cuts deeper than those offset by true cost savings must be recognized as a conscious reduction in Federal housing aid below levels now provided to the relatively small portion of low-income people who receive it. (Only about four million of the 23 million families who qualify under existing law actually receive any housing help. Most of the rest pay more than half their incomes for housing, much of which is substandard.)

State HFA experience, capacity, and proven housing programs may justify restricting housing block grants to States. States operate hundreds of ownership and rental housing programs which they have created to serve the entire spectrum of needy families, including the very low income, the homeless, the elderly, and the

disabled. States aggressively leverage public and private sector funds, work in partnership with localities, nonprofits, and the private sector, and coordinate and combine their many programs and resources to make maximum and most efficient use of them.

If local governments receive housing block grant funds, States should receive at least the 40 percent allocation the HOME Investment Partnership (HOME) program provides and should have the same flexibility HOME provides to invest their resources statewide. To the extent that the final congressional outcome reflects a greater apportionment of responsibility to States, the State share should be increased. For example, if a reduction in overall housing funding eliminates many local communities from participation in a State/local block grant program, the extent to which the State must pick up the funding burden for those disentitled communities must be taken into account by an increase in the State share. Congress should be mindful that the greater the number of jurisdictions receiving a share of limited Federal housing funds, the more diluted will be the capacity of any of them to have a meaningful impact.

Federal Housing Block Grants

Federal housing assistance not obligated under existing Federal contracts should be allocated under block grants, within broad guidelines for its use which Congress expressly provides. Section 42 of the Internal Revenue Code, which provides for the Federal Tax Credit, offers an effective model for this approach. The Tax Credit program provides maximum flexibility for each State to shape its own policy to its particular needs; has been nearly scandal free; and is effectively regulated through the full-time efforts of only a few Federal employees.

Another successful block grant model is the HOME program. Though still subject to more Federal regulation than is useful, HOME marks another bold step toward decentralizing decisions about affordable housing help to the States and localities. If HOME did not exist today and this Committee set out to create a program which mobilized private and public resources, under State and local direction, with limited Federal intrusion, to help finance privately owned, affordable homes and apartments for low-income renters and home buyers, you would create something much like HOME.

The Tax Credit and HOME work because they allow States and localities, not the Federal Government, to decide how to respond best to their unique housing needs and conditions. Similarly, any housing block grant you design should contain broad guidelines to protect the Federal interest, and sufficient accountability to assure that interest is fulfilled, but should carry no more strings than that. You will have accomplished little if you merely combine existing HUD programs with all their present burdens, limitations, and inefficiencies.

We urge you to consider the following block grant principles:

- Separate block grants with distinct Federal objectives and funding criteria should be established for affordable housing and community and economic development. Affordable housing needs cannot be measured by the same criteria as community and economic development needs. To combine them and subject them to a single distribution formula would cause inequitable funding outcomes and confuse Federal funding objectives.

  In addition, severe competition among States and localities to attract new business investment places a premium on community revitalization and economic development activities. Combining community and economic development funds with housing funds would inevitably crowd out Federal investment in affordable housing. Just as the Federal Government funds welfare and transportation programs separately to assure Federal investment in each, so should it maintain a separate commitment to affordable housing.

  In addition, combining these funds and distributing them among the nearly 1,000 local jurisdictions that now qualify for Community Development Block Grant (CDBG) funds would leave too little funding for communities to undertake any meaningful affordable housing effort. Also, many of the smaller communities would lack the capacity even if they had adequate resources.
- The affordable housing block grant should combine all Federal programs to acquire, build, renovate, and repair housing, including HOME, homeless, AIDS, elderly, and disabled housing programs. These funds should be consolidated simultaneously and not over time as HUD suggests.
- All tenant assistance funds (except public housing funds) should be consolidated into a separate block grant for the States to use in providing rental subsidies to tenants or to projects. Where the affordable housing supply is inadequate, jurisdictions should be free to invest some of these resources in housing repair or construction. In New York City, for example, 38 percent of families who receive a

Federal rent subsidy cannot locate an affordable house or apartment to use that subsidy to rent.

- All public housing programs should be folded into a fund administered by qualified PHA's to repair, operate, demolish, or replace projects, or to assist public housing tenants in the form of portable rent subsidies, as the PHA's judge appropriate. Troubled PHA's' funds should be redirected to the States or cities in which they are located.
- State housing block grant funds should be administered by State agencies designated by the governor.
- The formula for apportioning block grant money among States should be patterned after the HOME distribution formula.
- Housing block grant assistance should be limited to home buyers and owners whose incomes do not exceed 80 percent of the greater of the area or State median income, and to renters whose incomes do not exceed 60 percent, as in the present HOME program.
- Except for income targeting, States should be granted maximum flexibility to use block grant funds to design, structure, implement, and operate programs appropriate to their needs and conditions, including coordination of housing-programs with welfare programs.
- Funding set-asides or other prescriptive conditions should be rejected. Congressionally imposed rules for using housing funds which are block granted, including setting some funds aside for designated claimants such as nonprofits or the elderly, pose just as great a Federal tyranny as comparable rules imposed by bureaucrats.

  Decisions to direct funds to particular populations or through particular housing delivery systems should be left to the States. They are best able to judge need, cost-effectiveness, track record, and capacity. Some States, for example, have limited nonprofit capacity, and the use of third-party consultants to expand that capacity can drive up program costs.
- Since Federal funds to States are presently inadequate to meet their many needs and will almost certainly be reduced as Congress works to eliminate the budget deficit, no match should be required as a condition for States receiving block grant funds. States should decide how to use their own resources to respond best to their most pressing problems. If a State's overwhelming immediate need is in the welfare area, for example, its housing needs ought not be penalized if State funds required for a housing match are more urgently needed elsewhere.
- Congress should reject the performance-based funding which the HUD plan suggests. States' funding should not be held hostage to a set of federally designed standards that may be inappropriate measures of performance in any given State. Instead, States should be free to identify their housing needs and priorities, devise their own plans for meeting those needs, and be held accountable for demonstrating that Federal funds are expended in a manner consistent with Federal requirements.
- Jurisidictions should not be required to commit block grant funds to activities which Congress has not authorized or funded or may refuse to fund adequately under block grants in the future. For example, HUD proposes that several new activities be carried out through its proposed Affordable Housing Fund (AHF), including supportive services and service coordinators for the elderly, housing counseling, public housing modernization, and project-based rental assistance and operating subsidies, that were not authorized under the programs proposed for consolidation within the AHF.

Preserve the Essential Federal Role in Providing Mortgage Insurance

A continued Federal role in the provision of single and multifamily mortgage insurance is vital to providing affordable ownership and rental housing to lower income and underserved families and in all markets under all economic conditions. A decision to terminate the traditional Federal FHA mortgage function is a decision to cut off a whole economic class, and periodically entire regions, from mortgage insurance.

A continued Federal program is needed to provide insurance for the lowest income home buyers and in economically troubled areas, such as the oil patch and farm depression States of the 1980's, where the risks to private mortgage insurers outweigh the business rewards. For example, in 1993, 69 percent of FHA mortgages had down payments of less than 5 percent, compared to less than one-tenth of one percent of all mortgages purchased by the GSE's. Two-thirds of FHA loans in 1993 went to first-time home buyers, compared to only 30 percent of conventional loans (within FHA's mortgage limits). FHA insures twice as many loans for African-Americans as all private mortgage insurers combined. In the mid-1980's, the private mortgage in-

surance market share dropped from 41 to 9 percent in five oil patch States. Over the same period, FHA's market share in those States increased from 10 to 36 percent.

In 1993, two-thirds of all MRB mortgages made in 44 States were FHA insured. In 20 States, including Michigan, Florida, Connecticut, Texas, and Missouri, over 80 percent of all MRB mortgages were FHA insured that year.

Similarly, the termination of Federal multifamily mortgage insurance would severely limit the production of rental housing for lower-income families. Congress recognized this when, in 1992, it enacted a multifamily FHA/HFA risk-sharing demonstration program. In 1994, its first year of operation, 28 State HFA's qualified to participate in and nearly all of the 30,000 units authorized by Congress have been committed since. In Florida, for example, three projects consisting of 954 units are being developed through the risk-sharing program that would otherwise have been infeasible.

The FHA/HFA risk-sharing program is not, as some suggest, a revival of the failed co-insurance program of the 1980's. That program failed because participating lenders had minimal assets and nothing to risk, leading to irresponsible lending and inevitable losses. In contrast, State HFA's are State-chartered governmental agencies with the ability and incentive to assist HUD in their shared public missions of providing affordable housing, without taking undue risks with either their own or Federal assets. HFAs' track records in affordable housing lending are outstanding due to strong management and prudent underwriting. Twelve HFA's have requested, and received, "top tier" status from Standard and Poor's, recognizing the creditworthiness of their financings. No HFA has ever defaulted on a housing bond issue, and each agency has the implicit backing of its State government.

As State-chartered agencies, HFA's are subject to scrutiny equivalent to direct regulatory supervision. HFA's are held accountable by boards of directors which typically include high-level State government officials and private sector representatives. HFA's are audited annually, and their operations are closely monitored by the credit rating agencies, such as Moody's and Standard and Poor's, which rate their bond issues.

FHA's multifamily insurance program, however, should not be limited to risk-sharing with HFA's. That would exclude a number of fully competent States who simply lack the financial resources to participate in such arrangements.

The HUD Portfolio and Section 8 Housing

Before I conclude, I would like to turn for a moment to the State HFAs' concerns regarding Section 8 project-based assistance.

To reduce budget costs, HUD proposes not to renew expiring rental assistance contracts made to owners of apartments for low-income tenants. HUD also plans to seek authority from Congress to reduce some of its rental payments under existing contracts.

Under the Section 8 New Construction and Substantial Rehabilitation program, HUD has made long-term contracts with owners of more than 700,000 apartments. HUD agreed to pay the owners the difference between the rent specified in the contract and the rent affordable by a low- or very low-income tenant. Lenders relied on those contracts when they agreed to provide long-term mortgage financing for these projects. As many as 30 percent of these apartments were financed by State HFA's and significantly more by city and county housing agencies.

Most of these contracts are fixed for 20- to 40-year terms. Upon their termination, HUD plans to stop making rental assistance payments to the project owners. Thereafter, the owners will receive only the rents obtainable in whatever neighborhood the property is located. In some cases, that rent will be too little to maintain the building or to avoid a default on the mortgage. In many cases, that rent will be unaffordable to the projects' current tenants if no assistance is provided.

If such projects were financed with State or local bonds which are still outstanding, the government which issued the bonds would have to come up with the funds or default on the bonds. Fortunately, State governments issued few bonds for mortgages with terms exceeding the terms of the HUD rental assistance contract.

However, in most cases, the HUD contract on which States relied was structured so that it contained an initial term shorter than the mortgage, with periodic rights on the part of the owner and lender, to extend it without HUD's consent. Congress must make sure that these contracts are honored and funded. Otherwise, projects will default, State and local governments will be forced to absorb the losses or risk bond defaults, and the confidence of the capital markets will be severely undermined.

Some Section 8 mortgages-were insured by FHA. To avoid defaults on these federally insured properties when a contract expires, HUD proposes to pay off enough

of the mortgage so that the balance can be carried by whatever lower rent the owner can get. The State HFA's generally support this approach, although seriously question HUD's capacity and competence to perform the required financial analyses of the projects.

But the HUD plan contemplates no relief in the case of Section 8 mortgages which are not federally insured. When contracts on those properties expire, rents will fall to whatever rents unassisted tenants, if any, will pay. Projects with rents no longer adequate to service the mortgage debt or cover operating costs will default without some form of transitional assistance. Even if rents are adequate to sustain the property, they almost certainly will be unaffordable by the low-income tenants that presently occupy the project, causing those tenants to be displaced.

Tenant rental certificates or vouchers alone will not solve this problem. Certificate funding already is inadequate to the demand for it. Since certificates can only pay the difference between the market rent and that which the tenant can afford to pay, the subsidy may still be insufficient to support the project. Finally, in certain markets, certificate holders will be unable to locate alternative low-cost housing, and certain tenants, such as the elderly, who make up about 40 percent of the residency of such projects, will not want to move.

We urge the Congress to provide some sort of relief to such projects. The alternative is to lose thousands of apartments that are providing safe, decent, and affordable housing to needy families and to impose potentially severe financial hardship on HFA's—the very system on which the Congress intends to rely increasingly to deliver Federal housing assistance.

We also ask you not to enact the legislation HUD plans to seek repealing the 1987 Housing Act provision which prevents HUD from reducing rental payments under existing contracts. Some rents in some projects may produce income in excess of what is necessary to pay the mortgage and maintain the property. Rents in other projects do not. But HUD has not demonstrated the competence to make this determination fairly. If some rents are to be reduced, HUD must not have the unilateral power to do so. The views and consent of the affected lender should also be required.

The financial impact of granting HUD the power to reduce rents unilaterally would be serious. In Maryland, for example, a reduction of HUD-approved rents to neighborhood rents on a 110-unit elderly development in Hagerstown would cause a claim on the State's insurance fund of $4.9 million.

Thank your for this opportunity to testify.

PREPARED STATEMENT OF WILLIAM R. FREY

DIRECTOR, NEW YORK CITY OFFICE, THE ENTERPRISE FOUNDATION

APRIL 27, 1995

Chairman Mack, Senator Kerry, and Members of the Subcommittee, thank you for the opportunity to testify about proposals to restructure the Department of Housing and Urban Development (HUD). I am William Frey, the Director of the New York City Office of The Enterprise Foundation. As you consider reauthorizing Federal housing legislation, we appreciate your interest in understanding how community-based nonprofits are involved in and affected by the Federal structure.

The Enterprise Foundation

The Enterprise Foundation is a national nonprofit organization founded by Jim and Patty Rouse in 1982. Our mission is to see that all low-income Americans have access to fit and affordable housing so that they can move up and out of poverty and into the mainstream of American life. Enterprise is committed to creating affordable housing, rebuilding communities, demonstrating the possible, and finding innovative solutions to problems that plague low-income neighborhoods.

Enterprise works with community-based nonprofit groups to increase their capacity to provide low-income housing and help them build partnerships with State and local governments, and the private sector. Since 1982, we have invested over $1.2 billion in low-interest loans, grants and equity in the activities of more than 500 community-based nonprofits in 150 locations throughout the country. This investment has leveraged an additional $2 billion in financing.

We provide nonprofits with below-market interest rate loans primarily for, predevelopment and acquisition financing, as well as equity investments using the Low-Income Housing Tax Credit. We also offer guidance on how to link support services to those being housed to encourage self-sufficiency. The net result of this activity has been helping community-based nonprofits to develop more than 46,000

affordable homes for low-income people. Almost 40 percent of this housing serves residents with special needs, including senior citizens, formerly homeless families, and people with disabilities or HIV/AIDS.

The Enterprise Foundation's New York office was opened in 1987. Since that time, we have developed a new social partnership by bringing together 55 community-based nonprofit organizations throughout New York City's five boroughs, the city government, corporate investors and private philanthropists. With these partners, we have restored over 350 abandoned buildings and developed more than 5,000 apartments. We have housed nearly 11,000 people, 35 percent of whom were formerly homeless.

In New York, Enterprise has underway a significant home ownership program that complements our rental housing activity. The CityHome program is a partnership between New York City's Department of Housing Preservation and Development, The Community Preservation Corporation, several banks, and community-based organizations. Through CityHome, renovation and new construction are being used to provide over 250 one-to-four family homes for sale to low- and moderate-income families making between $20,000 and $45,000 a year.

In addition to housing activity, both The Enterprise Foundation's national program and the New York City program have a strong community service component. Issues of job creation, employment skills training and public safety are integral to our success in holistic neighborhood revitalization. In New York, we have created four Community Life Centers, which are located within or near low-income housing developments. The centers offer Montessori-style child care and a unique job training program that provides college accreditation.

Another example of the comprehensive revitalization activities that The Enterprise Foundation and its network of community-based groups are performing can be seen in Chairman Mack's home State of Florida. Enterprise works with 36 nonprofit organizations throughout the State of Florida. In 1985, Enterprise assisted in organizing Greater Miami Neighborhoods, Inc. (GMN). We continue to work closely with this organization. GMN offers financing and technical assistance to 20 Dade County nonprofits, including Little Haiti Housing Association, Miami Dade Neighborhood Housing Services, Nehemiah Project of Homestead, Centro Campesino Farmworkers Center, and the Urban League of Greater Miami. With these local groups, GMN has produced 800 homes for families with low incomes; another 1,574 homes are currently under construction or in the development stage.

As GMN's interest in and capacity for undertaking housing development grew, so did its support from the Miami business community. With corporate support from such investors as Barnett Bank of South Florida, Citibank, and the Fannie Mae Foundation, The Enterprise Social Investment Corporation (ESIC)—a finance subsidiary of The Enterprise Foundation—and GMN formed the Florida Equity Fund. To date, the Florida Equity Fund has raised $89 million in equity to be invested in Low-Income Housing Tax Credit projects. Leveraging this commitment of equity, an additional $130 million has been raised from private sources for affordable housing development in Florida. The Community Reinvestment Act has been a major catalyst for attracting these funds.

The Enterprise Foundation has embarked upon another major revitalization initiative in the Miami community of Overtown. Building on the success of our Neighborhood Transformation effort in the Sandtown-Winchester community of West Baltimore, we have begun to implement a neighborhood renewal program in Overtown. Neighborhood Transformation is a bold, comprehensive program designed to transform a decaying neighborhood into a viable community where residents can achieve their greatest potential. Such an approach must address all of the interrelated problems stifling prosperity in a low-income neighborhood.

Residents of Overtown, in addition to Overtown Neighborhood Partnerships and The Enterprise Foundation, kicked-off Overtown's community planning process in late February. Five planning groups will spend 6 months developing transformation strategies for health and human services, education, community building, physical development, and economic development. Initial efforts in Overtown include working with neighborhood community colleges to immunize every elementary school student in the community; creating a mentoring program through which Miami police officers adopt elementary school classes to provide special attention to students; and creating a "merchants' alliance" to provide assistance to local businesses in product development, marketing, loan packaging, and other essential services.

Urban Success Stories

These efforts help to illustrate that throughout the country there are many success stories about turning around distressed communities. Local, community-based initiatives have proven to be immensely successful in revitalizing everything from

single buildings to entire neighborhoods. Community-based nonprofits have tackled tough problems in cities all over the country and have a proven track record of efficient, creative solutions. By producing affordable housing, nonprofits can spur job creation and self-help in America's troubled inner-city neighborhoods because they are able to work in partnership with area residents, local governments, and the private sector to solve local problems.

All across the Nation, there are people helping others—to turn abandoned buildings into occupied ones, to seek entry level jobs, to set up quality child care so single parents can work, to provide primary health services, to drive out drugs and crime to hold the fragile glue of community together. Neighborhood-based nonprofit groups help serve basic human needs while demanding in return the responsibility that comes with assistance. Only an organization deeply rooted in the community, with links to local leaders and resources, could provide such conditional assistance.

The Federal Role

It is this decentralized approach to community-development that should be a touchstone for the Federal Government in determining its role in delivering housing and community development assistance. The Federal Government, specifically the Department of Housing and Urban Development (HUD), should not retain a structure of countless categorical programs with rigid directives. Instead, the Federal Government's role in the community revitalization process must be to provide a portion of the funding for community development initiatives and clear policy guidance necessary for local governments to target their resources to those most in need. The Federal Government must work in partnership with State and local governments and the private sector in an effective, nonbureaucratic way to rebuild communities.

Fostering successful community development efforts requires that Federal housing programs are given sufficient funding to achieve their objectives. A retraction of the Federal Government's investment in economic and community development activities saddles local governments with the largest unfunded mandate of all—the need for decent, affordable housing and healthier communities.

The Enterprise Foundation was founded 12 years ago with the mission of boosting the production of low-income housing by community-based nonprofits in partnership with local government, private business, *and* with support of the Federal Government. Only Government has the resources to meet the urgent needs of poor communities in a comprehensive fashion. Neither private charity nor private business can fill the void if the Government abandons its responsibilities. But Government also can't do it alone. The answer is partnerships that tap the ingenuity and know-how of the private sector enhanced by Government resources. The common theme in successful housing and community development initiatives is the right private sector partners joined with the Federal Government to make our communities better places to live, work and nurture families.

It is important to understand that most of the effective things that nonprofits do in the community development arena are contingent upon some contribution from the Federal Government. Nonprofit housing organizations are successfully blending Federal funding with private capital to develop quality affordable housing. In their work, nonprofits use a wide range of tools including the Low-Income Housing Tax Credit, the HOME program, FHA mortgage insurance, the Community Development Block Grant (CDBG) program, Section 8 rental assistance, the Federal Home Loan Bank System's Affordable Housing Program, State and local housing programs, and funds supplied by charitable foundations and religious institutions. These programs all work together to create a housing finance system that supports community revitalization efforts.

More than providing shelter, HUD programs play an important role in empowering communities, promoting community safety, creating jobs, and stimulating local economies. The Section 8 program is an example of a HUD resource that helps American families to move up and out of poverty. According to 1990 census data, one in ten American families pays more than one half of its annual income for rent. Section 8 rental assistance reduces the rent burden for such low-income families so that they have more money to spend on other necessities such as food, child care, and transportation. This rental assistance may also allow them to acquire savings for the future.

In addition to Federal programs, Federal policy has been critical to successful community development. The Community Reinvestment Act (CRA), working to assure that a bank helps to meet the credit needs of an entire community, is an essential building block of any community development strategy. CRA often spurs investments in Low-Income Housing Tax Credit projects, bank participation in lending consortia, and bank lending on affordable multifamily housing developments. Ac-

cording to current estimates, CRA has encouraged the investment of $60 billion in low- and moderate-income neighborhoods.

In order to solidify the Federal Government's commitment to urban redevelopment efforts, it is essential to retain HUD's status as a Cabinet-level agency. Urban centers and urban policy have been profoundly important to our country throughout its history. Despite recent shifts in population and wealth, 1990 data reveals that cities are still home to more than 77 percent of Americans, and more than 83 percent of the country's jobs. As accurately observed in HUD's recent report, *HUD Reinvention: From Blueprint to Action*, "Because of the inextricable links between central cities and suburban labor, housing and goods markets, economically healthy cities drive economically healthy metropolitan areas that are the building blocks of national economic growth." For all of these reasons, it is necessary to keep urban issues as a focal point of the United States Government.

To frame debate in terms of the abolition of HUD is to miss the point. We ought to be debating how to advance successful collaborations between the private sector and the government to improve cities. Proposals to eliminate HUD represent short-sighted thinking that would simply shift the costs of dealing with homelessness and other social problems into the budgets of prisons, and hospital emergency rooms. Federal commitment to housing and community development is crucial, and it must not be a scattered program through several agencies. For maximum efficiency and effectiveness, a Federal strategy must be focused where the parts can be made supportive of each other.

Congress and HUD should be working together to make the vision of HUD as a helpful partner for local initiatives a reality. In 1993, Congress and HUD together took bold steps to lay some of this groundwork. In accordance with the HUD Demonstration Act of 1993, HUD joined as a partner in the National Community Development Initiative (NCDI), the Nation's largest philanthropic collaboration for low-income neighborhood renewal in the country's history.

NCDI was developed in 1991 as a private partnership between seven of the Nation's leading foundations and a major insurance company to leverage the community-based work of LISC and Enterprise in a limited number of cities. Over its first 3-year round, NCDI made grants and low-interest loans totaling $62.5 million to scores of community-based nonprofits for neighborhood renewal in 20 cities including Baltimore, Boston, Dallas, Kansas City, Greater Miami, New York City, and Seattle. NCDI investments and contributions to local community development organizations are managed by The Enterprise Foundation and the Local Initiatives Support Corporation, which assures responsiveness to community goals.

As a result of Congress' hard work on the HUD Demonstration Act, HUD joined this collaboration, which has attracted more private partners and private financial resources. The second round of NCDI has mobilized an additional $87.7 million, including $20 million from HUD and $67.7 million from 10 private funders, to assist community development corporations in 23 cities across the country. This core funding is expected to generate more than $750 million in total funding for community revitalization when coupled with financial resources committed by over 200 local partners, including State and local government, local foundations, banks, and other corporations.

It is important to note that HUD is one of several funders participating in NCDI. Through this structure, HUD's role has been flexible and accountable to predetermined goals over a 3-year period. We believe this process is showing HUD a very different and exciting way of doing business, and that these terms have been crucial to attracting broad private funding. HUD's participation in NCDI offers an outstanding model for creating productive, nonbureaucratic partnerships between the public and private sectors.

The Reinvention Blueprint

HUD Secretary Cisneros' *Reinvention Blueprint* is very significant because it offers Congress many serious and substantive suggestions for making HUD a more constructive partner. In many cases, HUD's proposals make eminent sense. Because of its sheer scope, the *Reinvention Blueprint* will need to be examined, discussed, and debated in careful detail before Congress begins to restructure the Department. In any case, HUD should be commended for challenging the status quo and for forcing all participants in the debate—developers, lenders, owners, legislators, organizers, and advocates—to fully assess what is working and what is not.

Following is The Enterprise Foundation's evaluation of HUD's *Reinvention Blueprint:*

(1) PROGRAM CONSOLIDATION AND BLOCK GRANTS

Consolidating the multitude of HUD's programs makes sense, and Enterprise supports HUD's proposal to create the Affordable Housing Fund and the Community Opportunity Fund. Through the creation of these two funds, HUD has approached consolidation in a sensible manner. There is a clear recognition that one size does not fit all; HUD's housing function has deliberately been separated from its economic development function.

Similarly, any consolidation that Congress considers should be achieved along functional lines. Housing production, homeless activities, public housing operations and maintenance, and economic development activities *can* be distinctly different activities, and it is appropriate to retain separate funding streams for these activities. Within these broad categories, State and local governments and nonprofit organizations should be given great discretion about how funds are spent.

A streamlined and decentralized approach to housing programs should build on the success of HUD's HOME and Community Development Block Grant (CDBG) programs. Both HOME and CDBG have been flexible tools for State and local governments to finance neighborhood revitalization activities, allowing jurisdictions to determine how to best address local needs. Housing producers know these programs well and have used them successfully. They should be seen as the foundation of housing and economic development block grants, as HUD has proposed with the Affordable Housing Fund and Community Opportunity Fund.

Enterprise also supports HUD's proposal to retain essential features of current programs that have ensured the best use of limited Federal resources. The retention of the following requirements within block granted funding streams will ensure accountability of State and local program recipients:

Nonprofit Set-Aside

Under HUD's proposal for the Affordable Housing Fund, jurisdictions would be required to set aside 30 percent of their funds for all types of nonprofits, including sponsors of elderly and disabled housing and public housing authorities. One half of this set-aside, or 15 percent of funds, would be required to assist community-based nonprofit organizations.

Based on the experience of the HOME program, the nonprofit set-aside has been a critical tool for encouraging community-based solutions that address local needs. Community-based nonprofits are sensitive to the unique needs of their neighborhoods and their sustained commitment to the community makes them especially suited to undertake local development activities. Additionally, because nonprofits rely on many different sources of funding, they are able to leverage Government funding many times over to accomplish social goals.

Over the past decade, the nonprofit housing industry has expanded significantly both in production capacity and sophistication. Building the capacity of the nonprofit housing sector has been one of the main goals of the HOME program. In designing the program, policy makers wanted to produce housing that was responsive to the development needs of low- and moderate-income communities in which nonprofits already had an active stake. Congress wanted the residents of the communities served by nonprofits to participate, direct and have ownership in the housing that was developed with HOME funds. This involvement is happening throughout the country, and should not be wiped out in the process of program consolidation.

Income Targeting

Income targeting is another essential feature of any block grant program that Congress considers. Income targeting requirements within the HOME and CDBG programs have ensured that limited program dollars are spent on populations that are most in need of assistance. Recent data shows that more than half of all HOME funds assist families with incomes below 30 percent of area-median income; and more than 80 percent of funds benefit families with incomes below 50 percent of area-median income.

Congress requires that jurisdictions spend 70 percent of their CDBG funds to benefit low- and moderate-income people, however the 70 percent requirement is typically exceeded. In 1990, the average low- and moderate-income benefit across the country was 89 percent. To maximize the low-income investment, State and local governments often provide CDBG funds to community-based nonprofits to assist in their community development activities.

HUD's proposal for both the Affordable Housing Fund and the Community Opportunity Fund retains the income targeting requirements that currently exist within the HOME and CDBG programs. Experience shows that these targeting requirements have been very useful in steering State and local governments toward maximization of their Federal funds.

Homeless Housing

With respect to homeless housing, special attention must be paid to the substantial service component that is frequently involved in developing successful housing for homeless people. Enterprise assists in the development of a tremendous amount of service enriched housing for homeless people and is aware of the unique issues that arise in its developmental and operational stages.

Ideally, homeless housing should be maintained as a block grant separate from the Affordable Housing Fund to ensure that localities are addressing this dire problem in a comprehensive way. If Congress deems it appropriate to roll consolidated homeless funding into an affordable housing production block grant, a set-aside should be created for the specific purpose of providing housing and support services to this population.

(2) THE HOUSING CERTIFICATE FUND

The Enterprise Foundation does not agree with HUD's proposal to convert all project-based subsidies and public housing to tenant-based vouchers. It is our experience that, for the most part, the project-based Section 8 and public housing programs have worked quite well and that this success should not be discounted. It is also our perception that a mandate to "voucher out" these programs is contrary to other attempts (discussed above) to give localities flexibility to meet local needs. It is unlikely that a monolithic rental assistance program could be created that would meet communities' needs from Appalachia to Watts.

Project-based Section 8 Rental Assistance

Section 8 portable vouchers have provided very useful financial assistance to low-income people. They allow low-income people to move to fit housing closer to their jobs, and to move out of areas overly concentrated with low-income residents. Portable Section 8 vouchers can also be used by State and local governments to relocate people living in unfit structures that are suitable only for demolition, and for relocating residents while dealing with severely distressed public housing.

However, much evidence exists showing that the "mobility" concept is of limited practical value. First, many market areas have a shortage of affordable housing for families to choose. In addition to market realities, racial and economic discrimination have been major barriers to poor and minority families enjoying "freedom of choice" in residency. Finally, many low-income families are in need of housing that is deliberately located near such services as public transportation, day care, and job training and placement facilities. Portable vouchers do not ensure this proximity.

The unique value of project-based Section 8 rental assistance cannot be understated; project-based Section 8 serves a function that portable vouchers cannot. Project-based Section 8 has been critical to developing service-enriched supportive housing for "special needs" populations, such as the homeless, the mentally ill, and low-income people with AIDS. Supportive housing is permanent rental housing linked to a variety of support services, including primary health care and job placement, that allows otherwise limited residents to function independently. Without housing linked to such services, it is extremely difficult for formerly homeless and mentally ill individuals to become self-sufficient. Further, services are difficult to administer to such individuals without stable living environments.

Without project-based Section 8, it is nearly impossible to finance supportive housing development. Project-based Section 8 allows for a 15 year, dependable rent stream, which helps considerably to obtain debt financing. Without such a long-term, guaranteed rent stream, no private financial institution or State housing agency would finance the substantial physical cost of developing highly specialized housing. Additionally, Section 8 subsidies reduce the residents' rent burden, so that they do not have to pay more than 30 percent of their incomes. This allows supportive housing facilities to house very low-income people who, without the assistance of Section 8, would have great difficulty finding a place to live.

Public Housing

With regard to public housing, we again ask the Subcommittee to make a distinction between what is working and what is not. Enterprise's belief is that, for the most part, public housing offers decent shelter to low-income people across the country. In many cases, public housing has a lot to offer its residents, from day care services and educational and job skills training to a meaningful sense of community. Enterprise supports the early phases of HUD's proposal to address public housing—deregulating efficient public housing authorities (PHA's) and consolidating funding into a Public Housing Capital Fund and a Public Housing Operating Subsidies Fund. However, we oppose the ultimate stages of HUD's proposal, to roll public housing funding streams into the Housing Certificate Fund.

Enterprise concurs with HUD's recommendation that well-run PHA's should be deregulated and demolition criteria should be expanded. We also support the Appropriations Committee's repeal of the one-for-one hard replacement requirement. These substantial changes would allow successful PHA's to modernize their programs, and capitalize further on their success. Troubled PHA's that do not show promise should be placed into receivership immediately.

Over the past few years, Congress and HUD have shown innovation in dealing with severely distressed public housing owned and operated by PHA's that do show promise. The HOPE 6 Urban Revitalization Demonstration (URD) program to rehabilitate severely distressed public housing has great potential, and should be maintained as an eligible activity within the Public Housing Capital Fund. URD requires that one third of a recipient's severely distressed public housing units be replaced with 5-year tenant-based Section 8, and the balance be replaced through such means as scattered-site development or home ownership opportunities. At least 80 percent of an URD grant must be used for shelter, and up to 20 percent for community and social service activities.

In several cities where Enterprise works, opportunities like the URD program are bringing community-based nonprofits together with PHA's to rethink existing public housing opportunities. In many cases, these efforts will result in newly developed, low-density, mixed-income housing complemented with community services.

One example of this approach can be seen in Denver, where Enterprise has been working with Del Norte and Northeast Denver Housing, two local nonprofits with strong records of achievement, and the Denver PHA to expand opportunities for public housing residents. Based on a continuum of care model, these organizations are working together to devise a lease/purchase program so that public housing residents can graduate to become renters of privately owned homes, and eventually become homeowners themselves.

Preservation

The Enterprise Foundation has an interest in protecting the existing stock of HUD-assisted housing that is eligible for prepayment. This is a valuable supply of quality housing for people with low incomes. Several nonprofits are presently engaged in LIHPRHA transactions in such cities as Dallas, Miami, and Washington, DC.

Enterprise opposes the *Reinvention Blueprint's* proposal to give vouchers to residents who will be displaced when an owner prepays or raises rents to market rates in LIHPRHA-eligible properties. We are concerned that with all of the competing demands for vouchers, the preservation issue will not be adequately addressed with tenant-based rental assistance.

The National Housing Trust has been working with Congress and leaders in the field of preservation to devise a more efficient and less expensive way to preserve quality affordable housing than the LIHPRHA program. Preservation supporters are advocating for a capital grant or loan mechanism that would fund LIHPRHA transactions with a one-time capital grant to owners who sell their properties to nonprofits, or a one-time capital loan to owners who remain in the LIHPRHA program and refinance.

The capital grant/loan preserves valuable LIHPRHA housing stock for its remaining useful life while eliminating the need for new Section 8 in the property. This plan essentially divests the Federal Government of having to continually fund and manage LIHPRHA properties over many years. According to the National Housing Trust, this proposal is literally one-tenth of the cost of the present LIHPRHA program and would preserve over 115,000 units.

(3) CONVERSION OF FHA TO A GOVERNMENT-OWNED CORPORATION

The Enterprise Foundation supports HUD's proposal to transform the FHA into the Federal Housing Corporation (FHC), a Government-owned, market-driven corporation linked to HUD but freed from its current staffing and regulatory limitations. This proposal contains many features that will improve FHA's internal operations and expand upon its success as a primary mortgage insurer to low- and moderate-income families.

FHA, and other forms of Government-sponsored mortgage insurance, have traditionally filled an important niche in the housing finance system, for both single-family and multifamily housing. FHA has disproportionately helped minorities to achieve home ownership and has done a great deal to counter mortgage discrimination. Without adequate insurance or other credit enhancements, banks are given greater incentive to shy away from affordable housing lending.

In cities in which Enterprise works that have non-Federal multifamily insurance or credit enhancements available, nonprofit developers' success and productivity

stands in stark contrast to those cities without such resources. For example, Enterprise's New York City program has been very successful, in part, because of the State and city's longstanding commitment to developing low-income housing. In our first year, we were able to assist in the development of 1,000 units of housing because a bridge lender could insure its short-term loans through New York City's Real Estate Mortgage Insurance Corporation (REMIC). Without this insurance tool, in addition to New York State's mortgage insurance products, multifamily lending in New York would be vastly reduced.

Over its 60 year history, FHA also has been a pioneer in the housing finance system. FHA created new building, appraisal, underwriting, and other widely accepted market standards that are currently embraced by the private sector. FHA led the way in the development of long-term, self-amortizing mortgages and other products that are now traditional business products. And FHA has long made mortgage insurance available to underserved populations and in underserved neighborhoods, including central cities, in which private mortgage insurance companies have been reluctant to work.

However in recent history, FHA has encountered much difficulty. Outdated Federal acquisition guidelines and a shortage of staff in such critical areas as asset management have hampered FHA's ability to reach its full potential. Extraordinarily long processing periods and cumbersome paperwork also have served as detriments to finding financial institutions that are eager to make FHA loans. Nonetheless, the product that FHA offers provides the flexibility in underwriting that no other lender or insurer offers.

HUD's *Reinvention Blueprint* suggests a smart way to "modernize" FHA and its products to move beyond its current troubles and build upon its tradition of success. Conversion to a corporate structure that demands accountability without bureaucratic inefficiency makes great sense. The publicly chartered corporate structure builds on many prosperous models including Government-Sponsored Enterprises and housing finance agencies. FHA's shift to providing credit enhancement through risk-sharing with a variety of partners that are better able to respond to local needs, rather than offering retail services, expands on the success of the flourishing multifamily family risk-sharing program that was adopted by Congress in 1992.

The Enterprise Foundation's affiliate, Enterprise Mortgage Investments, Inc. (EMI) serves as a partner in a risk-sharing arrangement with Fannie Mae and can attest to the success of this model. Fannie Mae and Enterprise recently created a $150 million lending program that offers developers permanent first mortgages on primarily small projects that qualify for the Low-Income Housing Tax Credit. Enterprise formed EMI to serve as a community lender and provide this mortgage financing for affordable multifamily housing developments nationwide. Fannie Mae has approved EMI as a Special Fannie Mae Lender with fully delegated underwriting and servicing authority. It is EMI and Enterprise's solid understanding of local needs, real estate markets and affordable housing activities that allows Fannie Mae to deliver a better product.

Another positive component of HUD's proposal to modernize FHA is the consolidation of FHA's numerous insurance programs into three new authorities: single-family home ownership, multifamily rental housing, and health care facilities. Enterprise has long advocated for FHA to streamline its active programs and terminate its inactive ones. Such a reorganization would both make FHA much more workable for program users and would make internal program administration a far more simple task.

Finally, Enterprise wishes to bring to the Subcommittee's attention two provisions that HUD has made to assure that FHA is not delivering a product that is duplicative of the private mortgage insurance industry. The new FHC would be subject to two general limitations on its business: (1) a maximum mortgage amount, which would be set and adjusted at the FHA's current statutorily imposed limit; and (2) a 5-year aggregate new business limitation. These provisions would control the growth of a revitalized FHA, while allowing it to continue to serve the unique and very useful function it has served since 1934.

Portfolio Restructuring: "Mark-to-Market"

HUD makes a solid case for the need to restructure its portfolio, and the importance of separating HUD subsidies from insurance. As you. realize, the "mark-to-market" concept is highly technical, and may have many unintended consequences. Enterprise suggests that HUD proceed with a fairly large demonstration with this refinancing technique, which can be managed by State housing finance agencies. This would be a reasonable way determine the appropriate methodology and assess outcomes and unintended effects of such debt restructuring.

Conclusion

The Enterprise Foundation appreciates the opportunity to appear before this Subcommittee to discuss the work of community-based nonprofits and to evaluate HUD's Reinvention Blueprint. We look forward to working with this Subcommittee on housing reauthorization issues. Enterprise hopes that community-based nonprofits will continue to play a significant role in the Federal affordable housing delivery system into the future.

PREPARED STATEMENT OF DANETTE JONES

PRESIDENT AND EXECUTIVE DIRECTOR

MADISON PARK COMMUNITY DEVELOPMENT CORPORATION, BOSTON, MA

AND MEMBER, BOARD OF DIRECTORS

NATIONAL CONGRESS FOR COMMUNITY ECONOMIC DEVELOPMENT

APRIL 27, 1995

On behalf of the community economic development field, and the members and leaders of the National Congress for Community Economic Development, I would like to thank you for the opportunity to testify today before the Subcommittee on Housing Opportunity and Community Development on the future of community and economic development programs. We are encouraged that you are seeing the perspective of community development practitioners on the Department of Housing and Urban Development's proposed *Blueprint to Action*. This discussion and debate is both timely and necessary if we are to ensure that low- and moderate-income people are better served by our Nation's public and private sectors.

Over the past several months, we have closely followed the issues related to HUD's reinvention, and we have attempted, when appropriate, to provide some input on the issues shaping the current debate. We applaud both Secretary Henry Cisneros and the Members of this Committee for your earnest efforts to better serve our Nation's neediest citizens.

The Madison Park Development Corporation is a community development corporation serving residents of the Roxbury community of Boston, Massachusetts. Madison Park has been in existence for 28 years and has developed over 500 units of affordable, rental housing. We recently completed the $9.1 million rehabilitation and resyndication of a multi-family housing development and a $2.2 million rehabilitation of another housing project. A private, nonprofit corporation, Madison Park's success is directly attributable to its ability to leverage private dollars in order to maximize the impact of public investments.

The National Congress for Community Economic Development is the national trade association for the community development field with more than 2,000 community development corporations in its network and 23 State associations which serve as State affiliates. Community development corporations can be found in rural and urban areas of all 50 States and the Commonwealth of Puerto Rico and the Virgin Islands. Founded in 1970, NCCED encourages and supports its members through information, research, technical assistance, and capacity building.

According to a nationally recognized census due to be released next month, these community-based organizations—the Nation's 2,000 community development corporations—have produced nearly 400,000 units of affordable housing, created 67,000 full-time jobs, developed 23 million square feet of commercial and industrial space, and loaned $200 million to spur the creation of small businesses and entrepreneurial activities in some of the Nation's toughest communities.

As Congress searches for ways to streamline the Federal Government and eliminate wasteful, bureaucratic programs, it should keep in mind the proven capacity of these organizations to assist in rebuilding distressed neighborhoods. Rather than adding additional layers of bureaucracy, these organizations return control of the development process to local communities by allowing and encouraging the residents of these neighborhoods to address their community's problems by using market-driven solutions.

Last December, the Department of Housing and Urban Development announced that it would boldly go where few, if any, Federal agencies had ever gone before. Responding to growing criticism and threats of being dismantled, HUD proposed to reinvent itself as a leaner, more responsive, empowering, and performance-based Federal agency.

After several months of internal reflection, meetings and consultations with a broad array of interest groups, HUD has produced a document which, in some im-

portant ways, explains how the department will transform itself and become a better and "stronger partner of the American people and the communities in which they live." Speaking on behalf of the National Congress for Community Economic Development, I believe HUD deserves to be commended for displaying both vision and good faith in its efforts to reinvent itself. The *Blueprint to Action* is a thoughtful attempt to address and resolve some longstanding problems which had caused many people to become increasingly concerned and anxious about HUD's intentions and overall mission.

There are two major goals which I hope to accomplish during my presentation today. The first is to provide you with a practitioner's perspective on HUD's reinvention proposal, and how HUD's plans for consolidating and altering its programs will affect the community-based development field. The scope and breadth of HUD's, undertaking and its ramifications for the political, social, and economic structures of the Nation, reinforces HUD's continued existence as a cabinet level agency. Second, I want to offer some observations which HUD might find helpful in its efforts to insure the attainment of its objectives and possibly diminishing any public confusion once it has received legislative approval to implement the *Blueprint to Action*. The policy areas I will briefly discuss are program consolidation, block grants, local flexibility, performance-based standards, and housing vouchers.

There are some attractive features of the program consolidation plan. As a practitioner, the notion of dealing with one set of program regulations is appealing. In the past, coordinating multiple programs, each with their own distinct regulations, has been frustrating, costly, and time consuming. Placing these programs under one set of regulations would guarantee that service providers would make more efficient use of existing resources. It is important, however, not to discard regulations which currently insure that targeted populations receive the benefits they need.

The greater reliance on the use of block grants as a way of distributing HUD's funds and providing more autonomy to States and localities also poses some concerns for our field. We are not opposed, in principle, to the use of block grants. But we do believe it is important to recognize that given the proposed reductions in HUD's budget, the conversion of these funds into block grants actually represents a reduction in the resources being provided to low- and moderate-income communities. If we recondition and overhaul the current service delivery systems then we should be willing to spend more money in these critical areas.

Our national association will release a study next month reporting that the largest source of funding for community development corporations are Government block grants. Our field has developed the ability to access funding for community and housing development activities. It is important to note that much of this has happened because of Federal prescription and because the Federal Government has identified targeted deliverers of services such as community development corporations. Our field does not lack confidence in its ability to access resources under a decentralized system, but the Federal Government should not simply disperse fluids and assume that State and local governments are familiar with the organizations which best serve low- and moderate-income Americans.

The community-based development field for the past two decades has devoted a considerable amount of energy and resources educating the Federal system on the value of our work. Consequently, we are deeply concerned about the prospect of losing our forward momentum as a result of too suddenly shifting the entire responsibility for community-based development to States and localities.

NCCED strongly feels that the pursuit of maximum local flexibility should not come at the expense of delivering services to low-income communities. On the one hand, local flexibility often encourages greater public and private capital investment; rewards effective producers; and, provides necessary resources to the neediest people and communities. On the other hand, it also runs the risk of expanding local political patronage, thereby further disenfranchising low-income residents and opening up local programs to financial abuses and waste of precious public resources.

Performance-based standards are a step in the right direction. But while we encourage HUD's efforts to establish "performance categories," the implementation of these standards should not result in low-income residents from poorly performing localities losing funding for vital services if their city or town fails to achieve the performance measures contained in their local government's Consolidated Plan.

I agree with the goal of providing those Americans receiving public housing assistance with choice and flexibility; they have been trapped in living conditions which have diminished their quality of life. They have, in too many instances, been the victims of poor public policy decisions and heavy banded bureaucracy. As a public property manager, I am concerned about moving overnight to a universal voucher system. Project-based assistance needs to be improved, not eliminated. Our challenge is to continue to provide incentives for private investment while improving the

living conditions, potential for development of the residents, and maximizing the public investment in these projects.

In response to the public's demand for increased efficiency and accountability, HUD should examine the use of vouchers as part of an overall national strategy to provide low-income people with affordable housing. But this examination should be undertaken as part of a demonstration project in order to better develop performance and cost standards for such housing, and to create an effective process for overseeing and managing this part of HUD's portfolio. Full scale implementation of a national voucher program, absent any prior study, would result in displacing low-income families, further reductions of capital investment in neighborhoods, cash-flow problems for residential property owners and managers, destabilizing neighborhoods and the increased delay of refinancing and rehabilitation projects as investors and lenders reassess their investment and loan risks.

In conclusion, I would like to thank the Chairman and Members of the Subcommittee for the opportunity to better acquaint you with our work and our concerns regarding HUD's *Blueprint to Action*. I would like to reiterate that there is a network of over 2,000 community development corporations who applaud your leadership, commitment and resolve to improve the quality of life for our Nation's poorest and most distressed communities. We stand as a delivery system prepared to implement change, restore faith in Government, empower citizens, and shape a better future for our Nation.

Thank you for your time, attention, and consideration.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MACK FROM AUDLEY EVANS

Q.1. There has been increasing talk about including housing assistance in the broader context of comprehensive welfare reform. Some of the proposals include requiring residents, who are capable, to work for their housing benefits or to limit benefits to a certain period of time. What specific recommendations do you suggest for linking housing and welfare assistance so that we serve low-income families in a more coordinated fashion?

A.1. I do believe housing should be included in the broader context of comprehensive welfare reform. As a matter of fact, I think an analysis of all benefits should be done, thus determining the per person average subsidy received. After determining the average per person, then the individual should be notified of such total allowance. The individual should then be given the choice of how such total is spent, i.e., portion to food, health care, housing etc. based on the fact that different people have different needs.

To safeguard the integrity of the program, conditions of receipt should be established. For example: (1) From subsidy received, recipient must reside in housing that meets housing quality standards. (Thus the housing voucher program is validated.) (2) Recipients must participate, by payment in a health care program. (Government should require all insurance companies to pool resources to provide for indigent care enrollment at a reduced/subsidized rate, thus solving the health care crisis.) (3) Recipients should be required to be enrolled in school vocational/trade to receive benefits or are gainfully employed within 6 months.

To encourage employment, this benefit package should not be cut off as it is now, but be put on a sliding scale, that will encourage working. For example: If each benefit package is worth $1,500.00, and someone starts to work and earns $1,000.00, then such individual should not lose $1,000.00 in benefits but should be left (by means of a sliding scale) with residual benefits from this effort, therefore loss of benefit should be for argument sake $666.00, thus encouraging such individuals to continue working. Such scale when developed conceivably could provide benefits for life at a reduced rate and move up or down depending on the individuals success in the workplace.

To encourage working and micro business even more, the income tax system should exempt taxes on income to anyone earning at or below the national subsidized level as established in initial determination of current subsidy.

Q.2. Do you think there should be a time limit on housing assistance? If so, how do we assist families in becoming economically independent and self-sufficient members of society?

A.2. If my recommendation to Q.1. is adopted, then time limits will not be necessary, because the system will be effort driven.

If this is not adopted, then I do believe limits should be assigned with conditions. For example: A new resident (1st time) should be accepted for 1 year, during such time, the head of household should be required to report to agency efforts to either become gainfully employed or enrolled in school or job training. At the end of this year, if employment is found then a fair share rent (based on scale

to be determined) should be applied, and rental contract renewed for another year. Successive other reviews/evaluations should be condition of continued occupancy up to a period of 10 years. The elderly and persons legally or medically unable to work should be allowed housing assistance with no time limit.

If school enrollment or job training was the process followed, similar reviews/evaluations should be conducted as conditions of occupancy (terms to be determined).

This process will ensure accountability and stability and force upward mobility.

Q.3. What role should the Federal Government play in assisting those people who are unable to work to provide for themselves and their families?

A.3. My recommendation/answer to Q.1. provides this answer. There is a price per-recipient that is now paid. It is scattered over several agencies and departments. Consolidation of information will determine average individual subsidy. Such subsidy on a sliding scale will take in account the individuals described here, only difference is that such individuals will continue to receive maximum allowance all their lives. The upside is that such individual maximum will be capped at the national allowance per individual.

The great by-product from consolidation is that at the Federal, State, and other bureaucratic levels you will need less people to administer this program, therefore you could get rid of several departments.

Q.4. Can you briefly describe what impact the Davis-Bacon Law has had on the ability of your Housing Authority to hire residents to perform certain management functions? What chances to the Davis-Bacon Law would you recommend to encourage and expand entrepreneurial activities for your residents?

A.4. Davis-Bacon Law establishes minimum amounts to be paid to individuals to perform certain task during rehabilitation or construction on all our properties, but does not include management personnel. Such tasks are usually broad in scope and as such, by general description (taking into account full scope) requires the hiring of a licensed or skilled technician to perform duties and tasks.

In reality, within the specific undertaking, tasks could be broken down into functional items, thus allowing less skilled personnel at lower prices to perform parts of such tasks. Because wage determinations are in general describing the full task so as to relate it to a trade, you are restricted from paying less than approved, denying the less skilled the ability to participate.

Davis-Bacon in itself does not have a scale of wages to befit the capabilities of anyone other than journeyman. In many States in the southern region, there are very few apprenticeship opportunities for the construction trades. There needs to be a program directly linked to the Davis-Bacon wages that allows unskilled people the chance to learn a trade at reasonable wages.

With the Davis-Bacon restriction of only State approved apprenticeship programs being eligible for participation if there are no valid programs in your area, no learning process can be initiated so as to pay lessor wages for a task.

The averaging of Davis-Bacon wages is also important. Residents living in high profile union areas would be paid more than non-union areas. Davis-Bacon has historically used union wages in an area to establish their wages rates, this would leave residents who are learning a trade in nonunion areas making minimum wage and those in high profile union areas making 2 to 3 times that amount. The amount paid to learn individual trades should be comparable.

The changes to the Davis-Bacon Law that would encourage and expand entrepreneurial activities for residents are:

1. The ability of agencies to use people who want to learn a trade at reasonable rates.
2. Apprenticeship programs directly associated with Davis-Bacon Law to be developed locally.
3. The updating of wages in a specific area in a more timely manner.
4. Using Davis-Bacon wages as an averaging tool for the entire country not as a restricted area.

REINVENTION OF HUD AND REDIRECTION OF HOUSING POLICY

THURSDAY, MAY 4, 1995

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING OPPORTUNITY AND
COMMUNITY DEVELOPMENT, AND
SUBCOMMITTEE ON HUD OVERSIGHT AND STRUCTURE,
Washington, DC.

The Subcommittees met at 9:35 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Connie Mack (Chairman of the Subcommittee on Housing Opportunity and Community Development) and Senator Lauch Faircloth (Chairman of the Subcommittee on HUD Oversight and Structure) presiding.

OPENING STATEMENT OF SENATOR MACK

Senator MACK. The Subcommittee will come to order.

Welcome to the fourth of a series of hearings focused on the reorganization of HUD and the redirection of housing and community development policy.

Today's hearings focus on the mission and structure of the Federal Housing Administration, FHA. The FHA's single family insurance program has been one of the Federal Government's true success stories. Since its creation more than 60 years ago, FHA has insured more than 23 million mortgages on single-family homes, the majority of them first-time home buyers.

Last year, thanks to FHA's liberal underwriting standards and low-cash and downpayment requirements, approximately 450,000 families achieved home ownership for the first time using FHA insurance.

FHA particularly benefits those who do not have access to the traditional mortgage market. FHA's single-family insurance program is self-sustaining and thanks both to reforms enacted under Secretary Kemp's leadership and improved management, FHA appears to be financially solvent and actuarially sound.

The same cannot be said of HUD's multifamily insurance program, however.

FHA has estimated a $10 billion loan loss reserve against its multifamily portfolio of $44 billion.

That's a significant reserve, almost 25 percent.

An alarmingly high proportion of FHA's insured, subsidized, multifamily stock is distressed and many of FHA's multifamily programs, beginning in the 1940's through the coinsurance program of the 1980's, have been scandal-prone or otherwise discredited.

We will save a discussion of problems with the currently insured portfolio for a later time, but the question of whether there is a continued need for a HUD multifamily insurance program and whether HUD can acquire the capacity to run one are relevant to today's hearings.

We are having this discussion about the role of FHA because the mortgage market is changing. Sixty years ago, when FHA introduced the long-term, low downpayment mortgage, it was a pioneer.

But the world of housing finance has changed dramatically since FHA was created, especially in the last 15 years. More and more actors are engaged in the marketplace and they are offering services to a broader spectrum of the market. Government-sponsored housing enterprises, in particular, are playing an increasingly large role in that part of the marketplace once dominated by FHA.

For example, Fannie Mae now offers 3 percent downpayment mortgages and last year established a target of $1 trillion in new mortgages in 7 years. The lines that clearly divide the roles of HUD, the GSE's and the private mortgage insurance market are now being erased.

It is fair to ask what niche FHA has or should have in the current system of housing finance and the extent it competes or should compete against the other entities.

Some have suggested that FHA could be more effectively targeted to low- and moderate-income families and to geographic areas that are not well served by other mortgage programs. Others have suggested that the role of FHA should be credit enhancement, not the 100 percent insurance of individual mortgages. And still others have suggested that FHA has accomplished its missions and should be privatized.

Housing reform legislation proposed by HUD would create a Government-owned Federal housing corporation to replace the Federal Housing Administration. According to HUD, this new streamlined, business-oriented corporation would be more efficient than the current FHA and better able to respond to changing market conditions.

I do not reject the creation of a new corporate entity. However, I am concerned at least to this point. The discussion of the new Federal housing corporation has focused largely on corporate structure and not on the mission of FHA.

HUD has now at least proposed some quantitative measures by which its performance can be judged, but we need to know what HUD envisions as its role in the new housing finance marketplace before we focus on the organizational structure under which it intends to operate.

Structure is important. But to focus on structure before mission is to put the cart before the horse. Some of the questions we must ask here are as follows:

What unique market exists for FHA single-family services?

Is FHA still the best way to fill those niches in the market?

What other delivery options are available for meeting housing goals?

Should FHA be competing with them?

Should FHA be in the multifamily mortgage business?

After addressing the mission question, then it will be appropriate to ask whether a more autonomous structure is the most effective means of addressing capacity and management problems, what that structure should look like, and what its relationship should be with the rest of HUD.

We are pleased to welcome three witnesses today. Our lead-off witness is Nicolas Retsinas. We're delighted that you're with us.

Mr. RETSINAS. Thank you.

Senator MACK. The current Federal Housing Commissioner, who will address HUD's legislative proposal to create a Federal housing corporation.

Our second panel consists of G. Richard Dunnells, former HUD Deputy Assistant Secretary for Housing Management, and now a prominent real estate and housing finance attorney, and Stephen Moore, Director of Fiscal Policies at the CATO Institute.

I regret that a third invited witness on the second panel, former Federal Housing Commissioner Arthur J. Hill, was forced to cancel his appearance at the last moment because of a family medical emergency.

Again, we're delighted that you're with us and we look forward now to your testimony.

STATEMENT OF NICOLAS P. RETSINAS, FEDERAL HOUSING COMMISSIONER, ASSISTANT SECRETARY FOR HOUSING, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, WASHINGTON, DC

Mr. RETSINAS. Thank you, Mr. Chairman for giving us the opportunity to talk about a very important issue, which is home ownership and rental opportunities in this country. Thank you also for such a clear and comprehensive introduction.

Your report on the successes of the Federal Housing Administration are appropriate and duly noted. The importance of focusing on mission and fundamental questions as a preliminary to any discussion about delivery system is also fair.

What I would like to do with your permission is submit my written testimony for the record and really, if I could, share with you my observations, having now been in this position for a little less than 2 years, of the Federal Housing Administration, both its strengths, its weaknesses, its prospects, so we can begin to figure out together where it fits in a complex housing finance system.

As you point out, the Federal Housing Administration was created in 1934. I know you don't remember, and none of us remember, but if we tried to get a mortgage in 1934, generally speaking, you would need a downpayment of 50 percent. If you were lucky, you could get a 3- to 5-year interest-only note. When the dust settled, you took your chances in terms of refinancing.

Not surprisingly, as a result of that, there were very few homeowners in the country. About 4 out of 10 American families owned homes in the 1930's.

FHA, in the 1930's and the 1940's, revolutionized housing finance. It proved to the lending community, to the investor community, that investing in American families, providing long-term amortizing, fixed-rate mortgages made sense.

You're absolutely right. It has been such a success in now its 61-year history of the Federal Housing Administration, and it has not cost the Government any money. The single-family program has been self-sustaining.

The multifamily insurance program started later and had different goals and different objectives. And I'll talk more about that in a moment, about those differences and how it doesn't always have to be this way in terms of those differences.

Last spring, Secretary Cisneros, in looking at the Department, and specifically at FHA, asked me to address two questions.

No. 1, what's the mission of FHA today? Given the fact that the world has changed, is there still a mission? Is there still a role?

And No. 2, if there is, how do we best organize ourselves, how do we best cooperate to carry out that mission?

To help answer those questions, I convened forums and meetings around the country to talk to people, to talk to both current beneficiaries and users, but also to talk to organizations and individuals and groups that weren't users or beneficiaries of the FHA program.

In those eight hearings, we heard from 150 different people and organizations and we listened very carefully.

Let me share with you some of those conclusions.

I might add, parenthetically, this process to ensure the most rigor in the process was conducted through the auspices of the Harvard Joint Center for Housing Studies and they'll be, imminently, within the next week or two, issuing a final report on those forums. But let me, if I could, preview those conclusions.

Conclusion No. 1 is that, indeed, we really are the best house people in the world. That is, we look at the housing problems that exist in this country. If you compare it on any kind of international level, this country has been very successful in housing its people, If you look at home ownership rates, if you look at the condition of housing, the various standards that mark housing quality.

Conclusion No. 2 is, notwithstanding that observation, there continue to exist serious unmet housing needs in this country. They're not universal. There are particular places, there are particular groups of people who are most negatively affected by the current situation, that need more assistance, that have been left behind.

Conclusion No. 3 from those hearings was that for us to address, for we, as a Nation, we as a society, we as a Government, to address those unmet housing needs, there is a risk and there is subsidies that are inherent in addressing those needs.

It doesn't come painlessly. It doesn't come without cost.

It was our conclusion and the conclusion of these forums that to expect the private sector, independent of Government, to bear the risk, to pay the subsidy, to pay the cost, would not be able to address any legitimate or substantial way those unmet housing ways.

So, therefore, that argued for some continued kind of Government role.

Conclusion No. 4 was that, while our current way of doing business, I believe, and I honestly do believe this in my brief tenure, has served this Nation well, the 23 million homeowners that now exist, the over 4 million units that have been assisted through the multifamily program, the 85,000 hospital beds that have been in-

sured through this program, while it has served this country well, the world has indeed changed.

This is a different world than existed in 1934. There are different players. There are different actors in the world.

So it is encumbent upon us in this changing world to focus specifically on the issue of why an FHA? What is its mission? What is it that it is supposed to do? How can it as an entity add value to this housing finance mosaic that exists in the country?

There are different places. It is a continuum of assistance, but what's the FHA role?

I think we've identified and reaffirmed what that role is. No. 1, we believe a primary mission of FHA is to ensure that underserved and unserved people and places have access to affordable credit. We believe that is essential.

No. 2, we believe there continues to be an important role for FHA in demonstrating to the marketplace that it is possible to introduce new mortgage products that can address those needs and address them in a prudent way.

As in 1934, FHA proved, as history demonstrates, to the marketplace that long-term, fixed-rate mortgages, I might add, parenthetically, to a country that was still in the midst of a Depression, made sense and was worth doing.

We believe today there has continued to be a pioneering role that FHA can perform.

No. 3 is, generally speaking in this country, the economy is generally in good shape, through a lot of effort of you and your colleagues and our President. But at the same time, there are periods of time in certain parts of the country where the economy isn't in quite as good a shape.

We believe an important continuing mission of FHA is to be there when no one else is there, to be that underpinning of the economy, particularly of the real estate economy. And we believe having a vehicle to do that is critical as it relates to this country.

No. 4 is, to carry out those missions, we start with what I believe is a very legitimate parameter. The parameter is, and I want to focus for a moment on the single-family, though I think there are parallels for the multifamily, the parameter is, given what is the clear reality of budget shortfalls, of budget scarcity, of resource scarcity.

Senator I know you wrestle with that every day. Given those realities, and it's real—I may not wish it so. You may not wish it so. But it is real—it is unlikely that yet a new Government program will be introduced to pay for this risk in subsidy.

So, therefore, we believe it is important for FHA to continue to be self-sustaining.

One of the reasons it was such, as someone once described it, a jewel of the New Deal institutions, and they weren't all, but many of them were, is because of this focus on being self-sustaining.

As a matter of fact, you'll see in a moment when I talk about our legislative proposal, we believe, with a major qualification, which I will spell out, that we believe that we can create a multifamily insurance program that can also be self-sustaining. I have some evidence, I think, that gives you some comfort that that indeed is possible.

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Again, I might add for the record, just because you noted in your opening remarks, when I joined this Administration in the spring of 1993, as any new administrator would do, I called for the most comprehensive audit possible.

Any new administrator would start that.

The loan-loss reserve that we had created in 1993 wasn't $10.3 billion. It was $11.9 billion. But that was appropriate. That didn't mean the loss occurred overnight. It occurred over a period of time. But it was important for us to understand clearly what that loss was and act accordingly.

So we believe, to answer your first question, that, yes, there is a continued need for governmental involvement in housing finance. We believe the mission of making sure that credit and capital, which are the engines of neighborhood revitalization, are the engines of community revitalization, are available to people and places who are not served.

We believe there's a continuing role to pioneer and demonstrate to the marketplace what makes sense.

We believe there's a continuing role to be there when no one else wants to be there.

We believe there's a continuing role to provide a broad base of assistance so that we can be self-sustaining to do those first three missions.

The conclusion—one of the last conclusions of those forums was that even though one might say, one could conclude from those remarks that, well, if it's not broke, don't fix it, parts of it are broke.

Senator I wish I could say they are not.

Over time, FHA has been often more of a spectator on the mortgage marketplace than a participant. It is not often, it has not had that opportunity to add value in a way we think is creative.

We think the way to do that is to use the best practices of the private sector. I will give you—I see that the time is running out—I will give you some examples, if you'll allow me, in the question and answers, about some of the things we've done over the past year to use private-sector practices.

But we believe fundamentally that there is a public purpose mission and we believe fundamentally that public purpose mission is best addressed when this institution is accountable to the Government.

Having spent the last 20 years in and out of public service, I wish I could say that the traditional Government bureaucracy is the best way to exist in that marketplace.

But I've learned the hard way. I've learned the hard way that sometimes the processes and procedures that mark Government are indeed impediments to participating in a marketplace. Particularly a marketplace that should define our business as it relates to what the needs are.

We should be able to expand and contract as the marketplace as those needs evolved.

We believe that delivery system, in part, is this corporation.

The corporation, in all candor, Senator, is really just a way to get flexibility in the marketplace, to say that we believe in the principles, for example, the principles of procurement that say, go for low bid. Go for competition.

But the particular processes that the Government follows to reach that conclusion are cumbersome, are bulky.

It is interesting, as I watch and listen and participate to your efforts and your colleagues' efforts to deregulate, I often sit back and think, gee, I hope they start with us, in terms of the deregulation, so we can be held accountable.

We are prepared. In our legislation, we have set forth a series of performance goals. To impose those goals without flexibility gives people like me the excuse to point to other people and say, gee, I would have liked to have done it, but I couldn't get through this system. I couldn't get through that procedure. I couldn't get the right people.

We are prepared. I am prepared to be accountable to achieve that mission, to achieve those goals. But I think we need the flexibility to do so.

Let me just conclude for a moment on the multifamily because that's gotten a lot of attention and I know you said we'll have a separate discussion on that, so I don't want to talk so much about the budget implications.

In part, the multifamily insurance program is a victim of conflicting and overlapping objectives, all of which are worthwhile, I might add—the objective of preserving affordability, the objective of reaching out to those most in need.

But as a result, over the last decade, there has been an interlace of credit and subsidy.

For example, 75 percent of all our multifamily credit is linked to subsidies. So a simple solution of shutting the subsidies has a negative impact on the credit and on the obligation of the American taxpayer.

We have proposed, and again, we can go over it as you wish, this time or another time, we have proposed an approach, mark-to-market, which we believe begins to delink that subsidy in the credit.

I sincerely believe if we are able to figure that out to deal with this inherited liability, if we're able to figure that out, I believe we can create and define a multifamily insurance program that will respond to needs in the marketplace, will fill gaps in the marketplace and can be self-sustaining.

We've been doing some research recently on our multifamily credit and our preliminary results, and we will share with you within a week the final results, would indicate that that multifamily credit that was endorsed after tax reform, where people had to build projects on economics, not on taxes, because prior to that, much of the motivation was taxes, tax relief or tax benefits, that much of that has been self-sustaining.

As a matter of fact, there are lines of business in our multifamily that have been very profitable. And we believe if you look overall at the multifamily credit that has been endorsed after 1987, it has been generally close to break-even.

Some lines have been profitable. Some less than profitable.

That's not the case for the credit prior to 1987 and indeed, much of that liability.

So, in sum, we believe FHA has served an important function in this country. It has made home ownership possible. It has dem-

onstrated to the marketplace that it is worthwhile to invest in certain people and places.

But we also believe it's time to strengthen. We ought to strengthen from where we have been and not sort of turn our back.

Thank you, Mr. Chairman.

Senator MACK. Mr. Retsinas, I want to thank you for a particularly fine statement and want to indicate to you that we do look forward to working with you as we work our way through these issues.

But you've laid it out, I think, quite well this morning.

Senator Bond, do you have a statement you'd like to make before we get into the questions?

OPENING STATEMENT OF SENATOR BOND

Senator BOND. Thank you very much, Mr. Chairman. My apologies. There are two other hearings and meetings going on. I apologize for coming late. But I think it's very important that you called this hearing because this is our first opportunity to review publicly a number of the provisions in HUD's proposed reinvention legislation.

I particularly want to extend my thanks and my appreciation to Nic Retsinas for his hard work on the FHA corporation legislation. He's made great contributions to the debate on the FHA.

Having said that, I remain very much concerned that the proposed creation of the Federal housing corporation is premature. I think the FHA may need certain reforms to administer its programs and responsibilities in an effective and efficient manner.

I still believe the Congress needs to reassess the mission and the role of FHA mortgage insurance in the current real estate market.

In other words, who should FHA mortgage insurance serve and how should FHA mortgage insurance be improved, both as a program and a product?

In addition, how will these changes impact the private mortgage insurance market?

I worry, frankly, that this HUD proposal could end up disadvantaging and limiting the operation of the private marketplace. I'm also interested in understanding why Congress needs to create a new FHA corporation, as opposed to reforming the existing FHA statutes to make the FHA mortgage insurance programs more efficient and effective.

I need to review this year's Price-Waterhouse FHA audit. The FHA single-family mortgage insurance program is always at a risk of high defaults and losses because of high loan-to-value mortgages.

Is this a problem? And as Congress seeks to reduce the Federal deficit, I'm concerned about the extent of the risk to the taxpayer.

Before we make any major changes, I think we need to ensure that the FHA single-family mortgage insurance program is actuarially sound and is likely to remain so.

Finally, on the multifamily insurance programs, here, again, the mission, the need, and the risk to the Government are important issues and I remain very interested in a more complete understanding of the mark-to-market proposal. We've gone round and round and asked numerous questions and gotten more and more

clarifications. I am still, if not totally confused, at least three-quarters of the way there.

So, Mr. Chairman, I'm not going to be able to stay long, but I look forward to hearing some of your questions and staying as long as I can.

Senator MACK. Thank you, Senator Bond. And I think that we would be wise at this hearing, anyway, to avoid getting into the very complicated area of mark-to-market and maybe pursue that in a separate set of hearings and discussions.

Mr. RETSINAS. I wish I had that same option.

[Laughter.]

Senator MACK. Ours is just a matter of time, as opposed to whether we want to get into it or not.

I want to ask a series of questions related both to my opening statement and to the comments that you laid out.

The description of the Administration's proposal alludes to FHA's playing a future role in pioneering, which you clearly stated, and I think an important statement, in standardizing new mortgage products.

HUD provides only a rough framework, however, of its plans regarding the new single-family products it might offer, should it gain more independence from HUD.

Can you describe what types of new products might be offered should the legislative proposal be adopted?

Mr. RETSINAS. I can give you some examples, Senator, of what we have in mind.

Let me preface it by telling you the two questions we will ask about any new product.

No. 1, will it expand opportunities? Will it serve people and places that are not served now if the private sector is unable, or unwilling, to serve, for legitimate reasons? No. 2, will it be actuarially sound?

As I indicated, we start with the premise that this corporation needs to be self-sustaining if we can deal with that other problem that we're not going to talk about right now.

In the single-family area, let me give you some examples of products that we are talking about now.

I had the opportunity literally earlier this week, as an example, to visit Cleveland, Ohio, which is undergoing——

Senator MACK. Let me make a comment with respect to mark-to-market. If you want to get into it, if you want to spend the time here this morning, go right ahead. But I think it would not be helpful to the other issues we want to get to, the mission and the structure.

Mr. RETSINAS. I agree. No, absolutely. You're absolutely right, Senator, both of you, that it really needs the full attention because of the complexity.

In terms of the single-family products, let me give you a couple of examples.

The mortgage marketplace has evolved dramatically, particularly over the last 10 or 15 years. There are some products and some programs that the marketplace has not been able to respond to.

One example would be the lease purchase program, where lower income families, or individuals, but generally families, have an opportunity to rent and then own.

It has been very difficult for the marketplace to appropriately price that product.

We believe there would be an opportunity to find a way to do that. It may not have the same characteristics of standard FHA insurance today, but we think it could add value.

If I can put it in economic terms, if I might. As I look back, if I analyze, as I have, the role of FHA, in many ways, what it has done is demonstrate to the marketplace that the perceived risks, the market's perceived risk is greater than the real risk, and that's how it's been able to work, and that's how it's been able to be self-sustaining.

One example would be a product that insures lease/purchase or renter-own situations. Another would be the marketplace now for several years has taken advantage of the yield curve and they've come up with products such as the 7/23 mortgage, where there is a certain mortgage rate for 7 years and it's recalibrated at 23.

We believe there is a way to introduce that product to lower income and moderate income Americans. Right now, they're not often able to take advantage of that. That's another example of the kind of product.

There are a series of examples like that that we believe make sense. But, again, the screen will be, will it expand opportunity to unserved people and places and will it be actuarially sound?

So it's not anything goes, but we think there are examples of products.

There are similarly on the multifamily side, we can give you examples.

Senator MACK. In your opening comment, you referred to certain segments of the market, certain groups of people, certain geographic locations that, in essence, still remain underserved.

Mr. RETSINAS. Right.

Senator MACK. I wonder if you'd identify some of those for us.

Mr. RETSINAS. Sure. Some of them are amplifications of current markets we serve. Again, let me give you some examples and see if they suffice.

According to recent studies of both FHA insurance and the conventional marketplace, one of the areas that FHA has focused attention on, of course, and you point out in your opening statement, are individuals with insufficient resources to put together a downpayment to work in the conventional marketplace.

Let me give you a statistic that demonstrates that.

According to a recent study by our Office of Policy Development and Research, about 60 percent, about 59 percent of FHA mortgage insurance went to borrowers with a downpayment of less than 5 percent.

Now your reaction to that should be, well, of course. That's what it's in business to do. That ought not to surprise you.

What surprised me was the other statistic, was if you pulled that out and look at the conventional marketplace, pulling out FHA, the comparable statistic, that is, downpayments less than 5 percent,

not at 5 percent, was less than 1 percent. So it's a different kind of world.

We believe that there are a number of individuals, and I think, as an example, some new immigrants to this country who have different saving patterns, and we believe that we can find a way to extend the reach of the FHA program to apply those principles of a low downpayment to some of those groups.

So that would be one example.

Another group that's disproportionately served by FHA is minorities. Again, an example I hope will help illuminate the point.

A recent study indicated that in 1993, where we have sort of a full array of data, although I don't think 1994 is different, FHA approved roughly 2½ times as many mortgages to African-American homebuyers as every private mortgage insurance company combined.

So, again, I think it's been a focus on a different market. It's been a focus on a market of people with low downpayment, people with not standard credit, people who live in inner cities and rural areas. I think that's the market. And as I indicated from our forums, it is clear, there continue to be unmet housing needs in that regard.

Senator MACK. Well, I would hope that as you develop or expand those examples, I would really love to spend some time looking at those different niches, if you will, and trying to, in my own mind, conclude how those markets could best be served because that is the fundamental question.

Now, one other question that has more to do with kind of the geographic niche, if you will.

I think it was Steve Bartlett, the mayor of Dallas, who either in a separate conversation or during our hearing here, made the suggestion that there ought to be a greater focus by FHA to the inner-city. Have you done any work to determine how well FHA has done in penetrating the areas that have been redlined in this country?

Mr. RETSINAS. That's a good question. I want to answer in a couple of different ways because I was at a meeting last week in a major American city where one community group said, there has been too much FHA presence in a particular neighborhood.

It's in the category of you can't win.

In fact, I am not going to sit here and say that every FHA action, every FHA decision for 60 years has been a good one or a right one, sort of there have been more mistakes. There have been mistakes.

If you look at our statistics, if you look at the underserved areas statistics, as, again, one indicator of that, it's just a little short of twice the proportion of loans by FHA in those underserved areas as the marketplace as a whole.

I think where we have had a more difficult time penetrating——

Senator MACK. Would you say that a different way for me? I'm not sure I understood it.

Mr. RETSINAS. That if you look at the share of FHA lending in inner-city areas, that share, and I'll have to provide the specific numbers, is roughly just short of twice the share of conventional lending in those particular areas.

If I could just add one thing.

What I really would like to work with you and Senator Bond and others of, is I think where we don't have some of the same statistics and same impact has been in rural areas.

In part, it's because you've had a resource with the Farmers Home Administration, or formerly named—I don't know what it's called now—Farmers Home Administration. But it seems to me that we could make more of an impact there.

I had an opportunity recently to visit in Appalachia, and certainly, there are some critical housing needs there. And I think there is a role for us to play.

Senator MACK. I still want to go back to this issue about the inner cities.

Mr. RETSINAS. I've got the statistics, by the way, Senator.

Senator Mack. If you base your penetration of a market on roughly twice what the private sector has done, one of the big issues for many years with respect to mortgage lending has been the CRA, the redlining, because the private market has not provided the resources in the inner cities.

It's kind of like two times nothing is not a great number.

Mr. RETSINAS. It's 30 versus 15, by the way, just for the numbers.

Senator MACK. But the question is, is that real penetration?

Some have suggested that the lack of capital in the inner cities has been so great, that FHA's real mission should be in fact to be targeted more specifically in those areas.

How do you feel about that?

Mr. RETSINAS. I think the answer to that, a short answer to that, is we can target. We can target along any line you want—income, place, whatever it is. But there is a risk and a subsidy inherent in targeting.

Senator MACK. Listen, I fully understand and I think, again, that's what the private market has been saying. If FHA's mission in the past is to fill a gap that has failed to have been filled by the private sector, it may in fact point at the need for FHA to be more involved in the inner cities.

I'm not saying that's what the answer is, but I think it's really worth further discussion on it at this point.

Mr. RETSINAS. I agree, Senator.

Senator MACK. I'll turn to Senator Bond.

Senator BOND. OK. Thank you very much, Mr. Chairman. I've just gotten a call from my office that I've got to return.

Let me ask just a couple of questions, 3 questions in the hearing and I'll submit the rest of them for the record.

Nic, the types of households served by FHA depends largely on the nature of products that FHA offers, such as downpayment required and the underwriting standards used.

If FHA were to become an independent Government corporation, would changes in the mortgage products offered change the types of households served by the single-family program?

Mr. RETSINAS. Not change. I think it would expand the reach. There are still people that are unserved. And I believe with greater flexibility, we can expand that reach to those who are unserved.

There are more African-Americans that really ought to be owning a home.

Let me give you, again, Senator, I don't want to take your time, but one specific example.

We recently signed an agreement with the North Carolina Housing Finance Agency as a pilot that said, traditionally in this country, when we have underwritten single-family loans, you have looked at the concept of income and debt-to-income ratios. We have looked at income. We've said, well, a certain percentage of the income can be expected to be spent for housing costs and therefore, if that percentage equalled the mortgage, you get the mortgage, looking at other factors, but that's been the essential one.

It seems to me that's fair and it ought to be the general rule. But what about those situations where you do those calculations and you find out that that family, according to that percentage, can pay $400 a month?

Suppose that family says, "well, OK. But for the last 3 years, I've been renting and I've got good credit. I pay $600 a month for rent."

Could that not be a compensating factor?

So it seems to me that that's the kind of flexibility that allows us to reach people who now are not served.

Senator BOND. OK. The proposal for privatizing FHA, if we were to go that route, FHA might become the equivalent of another private mortgage insurer competing with existing private mortgage insurers.

What are the implications to the borrowers of privatizing FHA and how would it impact other private mortgage companies?

Mr. RETSINAS. That depends generally, of course, on the specifics of the proposal. But let me give you some general comments and principles.

Right now, private mortgage insurance companies can serve whoever qualifies, whoever are able to serve. It is ironic, again having administered FHA now for a little less than 2 years, one of the things that I always wonder about is FHA almost always costs more, almost always takes longer, despite my best efforts.

Maybe it's just the nature of Government. I don't know.

Given that, people apply for FHA and use FHA, not because they want to pay more, not because it takes longer, but because, generally speaking, they don't have other alternatives.

The concern that I think is fair for you to consider is any proposal that involves giving the private mortgage insurance companies that responsibility raises two questions.

One is who ends up paying for that? One way of doing that, of course, is increasing the premiums so much that it becomes self-sustaining within the payment base. But those who are least able to afford those increased premiums are those that we are most able to help.

Second, I would just caution all of us as we look at those proposals to remember one of the experiments that failed in the 1980's, which was the experiment of coinsurance.

It sounded good, but we found that when we delegated that responsibility, we are still paying that price, as we all know.

I think I would be careful in terms of affordability and in terms of added risk.

Senator BOND. Departing from that proposition somewhat, why did HUD reject the Office of Management and Budget's rec-

ommendation last fall that the FHA get out of insuring individual mortgages and rather, provide credit enhancement, say, in the form of loan-loss reserves to Fannie Mae or Freddie Mac or other securitizers?

Mr. RETSINAS. I'd like to talk about that, not in terms of who rejected what, but talk about that point.

Senator BOND. OK. Let's take the proposition.

Mr. RETSINAS. Right. If someone were to suggest that.

Senator BOND. If someone were to suggest that.

Mr. RETSINAS. Right. Because the administration——

Senator BOND. What would your response be?

Mr. RETSINAS. Our response would have been, if that were proposed, that thousands, perhaps a couple hundred thousand potential home buyers would not become homeowners.

It also said that, as I said to Senator Mack in my opening statement, that this is an important and complex housing finance system. There is a different role for different players of that system.

We believe that FHA, in its insurance, is an important undergirding of that system. And to risk that system at a time when we are all trying to reaffirm our commitment to home ownership, it's just too dangerous.

So it's the loss of affordability. It's the thousands, scores of homeowners who are left out of the marketplace. That would be a reason that I would be against such a proposal.

Senator BOND. You don't think it could be structured so that some type of credit enhancement, some kind of subsidy would enable those other agencies to reach that market that otherwise would not be reached?

Have you looked at that option?

Mr. RETSINAS. Yes, we have more than looked at the option because in our legislative proposal, one of the authorities that we're seeking is the authority to contemplate partnerships and risk-sharing partnerships.

Senator as you know, both of you come from States that have risk-sharing agreements with FHA for multifamily. And while the jury is still out, the preliminary results are very positive in that regard.

We would like the authority to pilot, to look at different kinds of partnerships.

As a matter of fact, in last year's legislation, we proposed such an authority. As we know, the bill didn't pass.

So I think there is some potential there. But to say, to throw away a program that has really served this country so well and take that risk that a new program works from scratch, I think is a proposition that we ought to be very careful about, Senator.

Senator BOND. Maybe we ought to be very careful about privatizing FHA, then, making it a Government corporation, by the same argument.

Mr. Chairman, Mr. Retsinas, my apologies, but I've got to run. We'll submit further questions for the record.

Mr. RETSINAS. Thank you, Senator.

Senator MACK. Thank you, Senator Bond.

I have a series of additional questions. But before we get into some questions about structure, just try one more time for me to

concisely say what you think the mission of FHA with this new structure will be because I think this issue about mission is so important.

If we're going to restructure, we ought to be saying up front really what that mission is going to be.

Mr. RETSINAS. The mission, No. 1, is to ensure that credit and capital is available to people and places who do not have access to affordable and accessible credit and capital, to make families who would not otherwise be homeowners, homeowners, to provide rental opportunities for people who are not decently housed.

So mission No. 1, is reaching out to those that the private sector, the private marketplace, is unable or unwilling to reach out to.

Senator MACK. Let me just again——

Mr. RETSINAS. Yes, sir.

Senator MACK. Do you feel that at this time you can be as clear in the delineation of what those niches are? And if so, could you try to do that now?

Mr. RETSINAS. Right. I believe I can, Senator.

They build upon the base of some of the existing beneficiaries. They build upon the base in our single-family area, of people who are unable to assemble the necessary downpayment to participate in the private marketplace.

They assist with people whose credit history and credit records would appear to be too risky for the private sector to be involved. And they particularly—not particularly, but they also address people who do not have, for lots of reasons, some appropriate, some inappropriate, access to the marketplace.

Again, I think of the minority participation.

I think those are three areas in the single-family.

In the multifamily area, these are products that the private sector, there are areas where the private sector perceives risk that far exceeds their risk tolerance.

For example, right now, in certain parts of the country, there are no nursing homes built unless they're FHA-insured because the private sector is concerned about health care and health reimbursement.

We also need to be concerned about that. But as an example, I told you about the study we're conducting. Nursing homes has been a profit center for the multifamily insurance program.

So we have been able to do it prudently and do it well.

The purpose of the corporation or the new structure is to allow us to more prudently and more responsibly make those determinations.

So you're right. It's a different question than mission. But we think it allows us to better carry out that mission.

Senator MACK. Do you think at this point you've made a relatively thorough statement of the mission?

Mr. RETSINAS. Yes.

Senator MACK. OK. I guess one of the questions, then, that comes up next is can you achieve your goal of making your programs more responsive to the marketplace by changing the existing structure of FHA, rather than creating an entirely new structure?

Mr. RETSINAS. In theory, yes, absolutely so. But I've been using an old Greek proverb, if I may, Senator, that you can't leap a canyon in two jumps.

Senator MACK. I like that.

Mr. RETSINAS. Thank you.

Senator MACK. Having been caught in attempting that second jump——

[Laughter.]

Mr. RETSINAS. It hurts a lot if you try to do it.

I guess part of it, Senator, and I'm going to be candid because I know that's what you want, is, over the last 2 years, we have tried to make incremental and marginal improvements.

In theory, the answer to your question is absolutely so. We can give you a list, and in the legislation, you'll see the specific relief we want from the specific provisions to do that.

So, in theory, the answer is yes.

I guess my own frustration is, over the past 2 years, is there's always a reason not to give relief from any individual provision. And what's been difficult is the problem is really the aggregation of all those impediments.

We believe the Government Corporations Act, which, as 40- or 50-year history, says that in certain situations, in situations where you have an organization that must exist in the marketplace, it makes sense to set it up with a corporate structure.

So the answer to your question is, in theory, yes. In practice, I'm not sure whether we would be able to assemble the relief we need from the various provisions.

Senator MACK. Why don't you tell us, then, what you think you're going to accomplish by making this change. Tell us a little bit about the kinds of problems you're trying to overcome.

Mr. RETSINAS. Again, if I could give you some examples of things, real examples of things that have happened.

When I joined the administration in 1993, as you recall, in 1993, our interest rates were relatively low, really at a historic low in many ways over the last 20 or 30 years.

It was clear to me, if we wanted to make some progress in dealing with our multifamily portfolio, I should do all that I could do to encourage refinancing.

As an insurer, that made abundant sense. It might not make sense as the lender, but as an insurer, it makes a lot of sense.

It took me 6 months to go through the process, not because anybody was against it. Everybody thought it was a good idea. It just took a long time to go through the process.

Now I would confess, Senator, in large measure, a lot of that is administrative because of the one-size-fits-all philosophy of our Federal Government.

But as a result, those 6 months saw a somewhat dramatic change in interest rates, and that was an opportunity lost.

Another example.

When I joined the administration and I did the audit you referred to before, one of the products of that audit that just shouted out at me was the fact that the Department was holding about 2500 multifamily notes that had been assigned to the Department,

many of them from that coinsurance program that I mentioned before.

Well, if I didn't know it then, I know it now—we're not very good landlords. There are some things we do well.

Being a landlord is not one of them.

One of the things I wanted to do is begin to package those notes, not as a fire sale, but to begin to put them into the hands of the private sector because I thought value could be added.

Again, it took me 9 months to go through the procurement process to hire a fiscal advisor to do that.

We finally did it and we put it together and we had a sale about a month ago that was very successful. It was so successful that we almost tripled our normal recovery rate on those kinds of properties. But we would have made even more if we had done it a year earlier.

Senator, it's really that, as you can hear, that frustration with that process that I hope and believe that a Government corporation could allow us to jump that canyon.

Senator MACK. What's going to happen with respect to the numbers of employees? Will you be—I suspect that there's going to be a pretty good sized reduction in the size of the operating staff in the new corporation. And I suspect that maybe some of the rules related to employment will be different.

Mr. RETSINAS. Correct.

Senator MACK. Will you be drawing on the present pool of FHA employees to staff this new corporation?

What kind of administrative transfers will take place? It sounds like, on the one hand, you also will be looking to bring in a different management team or a different group of administrators.

Could you share some thoughts with me on that?

Mr. RETSINAS. Your observations are correct. Secretary Cisneros has already indicated what our target staffing numbers would be, that we estimate that by the end of the decade, we would be down to 2500 employees in FHA, from a current 6,000, 6,000-plus, really.

In looking at that, clearly, we will look at our current employees and to try to provide opportunities for them within the new corporation.

Our proposal is that the employees of this Government corporation be Government employees, but they're employees of this new corporation.

The parallel, I would suggest, to give you a feel of what we're thinking about, is if you look at some of the flexibility that's inherent in the personnel systems of some of the bank regulators, FDIC, and the like, I think that's the kind of system that we envision.

There are some parallels, but you're absolutely right, some flexibility. And you're right. I believe that if we are to deal and operate reflective of the magnitude of the assets that we watch over—we now have $380 billion of insurance in force—yes, we need to bring in some new skills to help manage that and complete things like those note sales.

We ought not to be, as I say, a landlord, but get out of that business.

Senator MACK. I may get back more to the structure in a moment.

Mr. RETSINAS. Yes, sir.

Senator MACK. But I want to ask a question that I think has been touched on, but I just want to go into a little bit more detail on it.

While I've recognized and both agree that there are niches in the marketplace that FHA should be servicing, there's no question, though, that the private market is becoming more aggressive in moving into making low downpayment mortgages and so forth.

That raises the question of what kind of competition is going to, what's going to take place between, say, this new corporation, and an expanding private-market effort to get into the types of mortgage loans that FHA has been insuring.

How do you see that playing out? What kind of impact does that have?

Mr. RETSINAS. That's a good question.

Right now, if—let me just respond with a rhetorical thought and then specifically answer your question.

I have many different hats at the Department. One of the hats is Federal Housing Commissioner. But I am also the Assistant Secretary for Housing.

I recall several months ago, I was at a press conference and someone asked me about one of these new initiatives from one of the private mortgage insurance companies, a lower downpayment, a pilot program.

All of these programs are relatively small in the marketplace. And my answer was I applaud it. I applaud it.

My job, on your behalf, is to make sure this country is as well housed as it could possibly be and make sure we increase the home ownership rate in this country, for all the obvious reasons.

So I applaud that.

I sometimes wonder that in the absence of FHA, how many of these initiatives would take place. I believe there is a role, a corollary role for an FHA in keeping the marketplace stretching to address some of these needs.

Senator MACK. Listen, I agree. In fact, that's exactly the reason that I asked the question.

The point that you made, starting 60 years ago, 61 years ago, is that FHA pioneered and, in essence, said to the private market, boy, this can be a profitable business and we have seen over the years that the private marketplace has in fact been responding.

The question is, is it going to be responding to the point that it takes some of your business away and some of that being profitable?

Mr. RETSINAS. I wish—I gave you the statistics before about the relative percentages, the low downpayment. I guess I wish we had done a better job proving that under 5 percent downpayment works, so we get more than 1 percent of the marketplace.

But in terms of the competition question, let me tell you how we're responding to it in the legislation, though it's something clearly that we're prepared to work on more.

I believe that the corporation ought to have performance goals. Those performance goals ought to be to that primary mission that I indicated before, underserved and unserved people and places.

I believe that focus on mission would reduce substantially any—not any—would reduce substantially interest in competition because the measure will be, the measure, I believe, Mr. Chairman, respectfully, I believe the measure ought to be for the corporation is the unmet housing needs we serve.

I often get questions, well, the measure ought to be how many loans you insure.

No, I don't think so. I don't think that's the right measure. I think the measure is what needs are addressed. Are we helping people who the private sector is not prepared to address?

Now, is there at the margin some borderline loans that maybe could go either way? Perhaps. But I think, generally, as you look at the statistics, there really hasn't been competition.

Again, 60 percent versus 1 percent. It's 50 percent, 2½ times the total.

So I think that they've been different.

Now, I certainly, by the way, in saying that would encourage, applaud, welcome and solicit private mortgage insurance companies, Government-Sponsored Enterprises, to do more at that low end.

There are unmet housing needs in this country. You and I know it. So there's plenty of room to do that, and I would certainly welcome it and solicit it.

Senator MACK. So you don't really see the competition thing as being, at least in the short range, anything of significance.

Mr. RETSINAS. Of being a major issue, that's correct.

Senator MACK. I think that we have seen some specific kind of target numbers that you all have given us as to the kinds of things you want to focus in on.

Mr. RETSINAS. Right.

Senator MACK. I wonder if you could tell me how well FHA has done at present in reaching kind of those targets that you've established.

Mr. RETSINAS. The targets generally reflect an extrapolation of the current portfolio.

So we have generally been able to meet those targets. It depends, obviously, on the definitions, to what extent single-family and multifamily are combined and some of that data and the like.

I think FHA's track record has been substantial, has been positive.

Could it do more? Does it need to do more? Yes. Absolutely.

Senator MACK. Let me make sure I understand this.

Mr. RETSINAS. Sure.

Senator MACK. You're saying that, basically, FHA has met the kind of targets that you've established for this new corporation.

Mr. RETSINAS. Right. The targets are transitional targets because we believe the targets ought to be refined. The targets perhaps ought to be modified based on our increased capacity under a new corporation.

In many ways, Senator, the target model—I'm not sure that's the right expression—but the model of the targets parallels some of the work that you and your colleagues did on the GSE legislation, which is providing a transitional year to help figure out how best to address what are appropriate goals. How do you balance prudence and, in this case, mission?

Senator MACK. So the mission targets or the targets for the mission of the new corporation are not that different than what you would hope FHA——

Mr. RETSINAS. Right, during the transitional period, yes.

Senator MACK. Are future targets going to be reflected in your business plan?

Mr. RETSINAS. Yes.

Senator MACK. And when will we see that?

Mr. RETSINAS. We are working on a business plan now. We have a preliminary draft of the business plan. But my guess is it's weeks away.

A business plan, like anything else, continues to evolve. But we are certainly in the middle of working on it right now.

Senator MACK. And what kind of differences do you think we might see as far as these?

Mr. RETSINAS. Oh, I think, I would certainly propose during a transitional year we go with the targets that we have proposed because it is transitional.

Senator MACK. Let me get us into some more discussion on the multifamily issue.

Over the years, HUD's multifamily insurance programs have cost the taxpayers billions of dollars to cover insurance losses.

Mr. RETSINAS. Yes, sir.

Senator MACK. HUD is clearly banking on the fact that investments in staffing and information systems can break the cycle of waste, abuse and mismanagement.

But given HUD's track record, why should Congress be more willing to invest in multifamily insurance programs?

Can these programs be made actuarially sound?

And I realize you've already touched on some of that. But, again, this issue is multifamily insurance and I guess, particularly in light of the fact of the $10 billion loan reserve.

Mr. RETSINAS. $10 billion, right.

Senator MACK. Against a $44 billion package, it really raises some very, very serious questions.

So I think it's important that you address that.

Mr. RETSINAS. Yes. I thank you for that opportunity, Senator. You're absolutely right.

If you look at the origins of the loan-loss reserve, there are many factors. And I'm not here certainly to point fingers. But a good part of that loan-loss reserve comes from the coinsurance program—well-intended, I am sure, but its execution left much to be desired.

A good part of that loan-loss reserve came from the fact that the multifamily marketplace in the 1980's, as we are all painfully aware, went through a grave transition. Lending institutions, generally, lost money because of commercial and multifamily investments over time.

Part of it comes from decisions that were made that were really more subsidy-driven rather than credit-driven.

As I indicated, we have looked closely at the multifamily program and we believe not only that there continues to be a need, and I'm going to give you some examples in a second. But more importantly, we believe that we can design a program that will have

the same track record of self-sustainability as the single-family program has had.

We recently have been looking at data which I will share with you, and I think this is days away, share with you, looking at the insurance endorsements after tax reform, because, as I indicated earlier, in my reflection, having been in the real estate business now for several years, I dare say, many people invested in housing, they didn't really know that they were investing in housing. They were investing in tax shelters.

Tax reform began to change the equation. Tax reform said, and I certainly applaud the Congress for the general thrust of tax reform, that we ought to consider investment decisions on the economics. Look at how much money it costs, how much money you make and let it work that way. Let's really look at it.

If you look at our insurance and the endorsements since1987, generally speaking, they have been, and it varies product line to product line, but generally speaking, they have either made money or been self-sustaining.

Not all, and we'll share that with you line by line.

I believe, through creative partnerships, through being prudent in terms of the kinds of products, that need can continue to be served.

Let me give you again some examples.

There is, you know, we all know, about the demographic changes that are undergoing in this country in terms of the aging of the population and the kinds of services they require as you wrestle with health care and all of those attendant issues.

It's clear to us that products such as assisted living facilities can make an important contribution. The private sector has, generally speaking, not been able to come up with mortgage products that have been able to appropriately price the risk that's inherent in those kinds of efforts.

We believe a new FHA could demonstrate to that marketplace that those kinds of products make sense.

There are also parts of the country that are so underserved, that certain markets just stay out of it. Again, an example.

Hospitals. A lot of people don't know it, but we also insure hospitals. That has been a profit center for FHA. There are parts of the country, parts of the Northeast, for example, where no one is financing hospitals.

Senator MACK. I find that particularly interesting. I was involved in the development and construction of a new hospital in my hometown years ago. Someone reminded me the other day it was 20 years ago, which shocked me.

One of the areas of financing that we considered was FHA. And so we got into some discussions here with the staff when we were preparing for the hearings and I was really kind of stunned.

I think the overwhelming hospital financing, FHA financing, is like in New York and maybe one other State.

Mr. RETSINAS. New York and New Jersey currently, correct.

Senator MACK. Yes. Why is it that one State or two States would somehow not find private sources of capital for hospital construction?

I must say to you that, having been a lender, I spent 16 years in the banking business and I have a tendency to believe that markets tell us things.

What's New York and New Jersey saying about the financing of hospitals that maybe FHA ought to be concerned about?

Mr. RETSINAS. I think what the market is telling us, that there is—and I'm speculating. I don't want to speak for the market, obviously, on the capital markets in this regard.

But I think what they're telling us is they assess health care reimbursement in the Northeast and in those particular States. They have enough of a concern over time to question whether they're prepared to provide any long-term credit enhancement to that.

It is the marketplace. The thing with FHA, unlike lots of other Government programs, is we don't seek the business. People aren't entitled. People apply.

We have received, I might add, recently applications from other parts of the country. We have an application pending from Chicago.

Anecdotally—but you're absolutely right. In recent years, the focus has been on New York and New Jersey. But even more exclusively, on New York.

Now, if you look at the track record, as insurance company premiums versus claims, net of holding costs, it's been very profitable.

I might add, I believe, and don't hold me to this, but I believe if it's not the most profitable line, it's the next to most profitable line of all the multifamily insurance.

Senator MACK. And that's judged over what period of time?

Mr. RETSINAS. In its history.

Senator MACK. You're talking about the hospital financing.

Mr. RETSINAS. Hospital insurance program, right.

Senator MACK. Interesting.

Mr. RETSINAS. I can give you more specifics.

Senator MACK. I broke in there on a previous question. Frankly, I've forgotten where we were. I don't know if you remember where we were or not.

Mr. RETSINAS. No, I don't, Senator. I'm sorry.

Senator MACK. We were talking about the multifamily insurance program.

Mr. RETSINAS. Yes, sir.

Senator MACK. I think you were in fact kind of beginning to touch on the importance of FHA in the multifamily.

That raises another area. The FHA's share of the multifamily insurance market is relatively small. Frankly, people are looking at ending the multifamily credit subsidy as a potential budget savings.

What would be the practical effect of HUD getting out of the multifamily insurance business?

Mr. RETSINAS. I think the practical effect, there would be certain products in certain areas that would not be served.

Like in the single-family program, there is nothing now stopping the private marketplace from insuring multifamily housing or health care facilities.

But as I look around the country, there are certain areas where, for example, no more nursing homes would be built. In New York State, we just used the example of hospitals. I don't want to be so

definitive, but it's unlikely any hospitals would be modernized or expanded or financed absent FHA.

I think, in addition, while the share is low, it's not a question of share. It's also a function of need.

One of the real gaps, I believe, in the marketplace is assistance in the financing of small properties, the development of small properties and the rehabilitation of small properties.

The FHA process is a bulky and cumbersome one that doesn't generally lend itself to small properties.

One of the new products that we would like to consider is a product to ensure small properties. Perhaps in conjunction, for example, with local community development corporations.

Senator MACK. Give me a sense of what you mean by small properties.

Mr. RETSINAS. Oh, it could be a property under 20 units. It could be a 12-unit or 15-unit or small garden apartment, those kinds of properties.

It would vary, obviously, from place to place.

Senator MACK. Let me just look through here and get a sense of where we're at.

[Pause.]

Frankly, we've covered a lot of ground here this morning. There may be other questions. There are a lot of other specific questions here. But I think that, frankly, we've gone on long enough and you've been very, very helpful.

I think what we'll do is go through these questions that we had that we didn't raise this morning and maybe get those to you and ask you to respond to those in writing.

Again, I appreciate the testimony that you've given this morning. I thought that your opening statement was, again, excellent.

Mr. RETSINAS. Thank you, sir.

Senator MACK. And I look forward to working with you.

I think this is an important question and deserves a lot of time, and we will eventually get to the issue of the mark-to-market.

Thank you for being here this morning.

Mr. RETSINAS. Senator, thank you and I appreciate your gracious comments.

These are complex issues, all the issues that we talked about. And I'm prepared to be at your service in helping to figure out the right answers.

Senator MACK. Very good.

Mr. RETSINAS. Thank you, Senator.

Senator MACK. Mr. Dunnells and Mr. Moore.

Again, I want to welcome both of you and I thank you for taking the time to be with us this morning. I think that you—I know that Mr. Dunnells was here during the entire time. I don't know whether Mr. Moore was or not. But I appreciate your being here and Mr. Moore, why don't you go ahead and we'll start with you, and then, Mr. Dunnells, with you.

STATEMENT OF STEPHEN MOORE, DIRECTOR OF FISCAL POLICY STUDIES, THE CATO INSTITUTE, WASHINGTON, DC

Mr. MOORE. Thank you, Senator, and thank you for the opportunity to testify.

I think we're asking the right question today—what is the mission of the FHA.

Mr. Retsinas mentioned, of course, that the FHA was created in the 1930's. I think few would argue that when the FHA was created and probably for about its first 50 years, FHA played a vital role in serving the low-income community in terms of bringing housing to a lot of neighborhoods and to a lot of American homeowners.

I would argue, however, just to state my point from the start, that it is time to start thinking seriously about privatizing FHA.

And I would say that we should privatize the FHA basically for three reasons.

First, I think more and more the FHA is competing with a vibrant and productive private marketplace and that more and more, it is trying to expand or retain its market share, I think, by taking on riskier and riskier loans. And as a taxpayer, I think that that's something that we have to be very concerned about.

The second point that I would make about FHA is that, as I look at the evidence in terms of the kinds of loans that FHA is making, the FHA has strayed from its original mission, which was to serve low-income and moderate-income housing markets.

One good piece of evidence with respect to this is the size of the cap with respect to the mortgages. Right now, in high housing market areas, it's $153,000. And a lot of the interest groups have been promoting raising that to$200,000.

Now that, Senator Mack, is not a low-income or even a moderate-income market, I would argue.

Finally, and this is the most important point, that I believe that the FHA can only continue to retain its market share in the mortgage insurance business by taking on riskier and riskier loans. And in fact, we're seeing this done.

If you look over the last 10 years, actually, about the last 15 years, in 1978, the average downpayment on FHA loans was about 10 percent. Today, it's less than 5 percent.

That is the average person taking out an FHA-insured mortgage is putting less than 5 percent down.

Now why should we be concerned about this?

The reason is very simple—the single most important factor in determining whether a loan is sound and whether it's likely to go into default or delinquency is the size of the downpayment.

Studies show that in fact, there's sort of a rule of thumb that when you reduce the downpayment by half, you double the risk on the loan. And that's something that we should be very concerned about.

Now let me mention a little bit about my history with dealing with this program, Senator.

I got involved in this area in about 1985, when I used to work at the Heritage Foundation. We issued a paper back then arguing that the FHA was a ticking time bomb, that a lot of the sloppy management practices and a lot of the very risky types of lending practices that were taking place at the FHA were leading us to what we called the ticking time bomb that would soon explode into the taxpayers.

Senator MACK. Let me ask you a question. Did you make a distinction between multifamily and single-family when you made that——

Mr. MOORE. We were talking about the single-family program. And the multifamily is even worse. But we were looking mainly at the single-family.

The reason I bring up this whole incident, I think it's important because we did say that this is a program that's in great jeopardy of large losses.

What happened when we issued that study, it came out in about June 1986, is that it was vilified by virtually everyone who looked at it. That is—well, it was interesting who vilified it.

It was not vilified by low-income groups. It was not vilified by minority groups and so forth, who are supposedly being served by FHA.

The people who vilified the study were the mortgage bankers, the realtors, the construction industry—that is the housing industry.

From that experience—and by the way, let me just say that one of the reasons that FHA has improved somewhat since then—and by the way, as you know, in 1987, that's when the time bomb did explode and FHA lost $1.4 billion.

At that time, though, the mortgage bankers said we're totally exaggerating about the situation and there is not going to be any losses. This is hyperbole, and so on and so forth.

I think that what I learned from that experience is who the real beneficiaries of this program are.

I think it's very clear that this is a program that has been captured over the years by the special interest groups. And interestingly enough, one of the things that we've been doing at CATO over the last year to help the House Republicans is to put together a package of corporate welfare reductions.

The more and more I got involved in this project, the more I realized that FHA is one of those programs that should be on that list because there's no question that the kinds of groups that are the main beneficiaries of FHA are mortgage bankers and realtors.

Now let me very quickly get to this question of do we still need an FHA?

I would like to, if I may, just read to you, because you asked the previous speaker quite often about what should be the mission of the FHA. And I'd like to read to you a quote from the 1948 Federal Housing Policy Act, which I think very succinctly summarizes what the FHA mission should be.

It says that the policy to be followed in attaining the National housing objective hereby established shall be, one, private enterprise shall be encouraged to serve as large a part of the total need as it can; and two, Government assistance shall be utilized, where feasible, to enable private enterprise to serve more of the total need.

I think that's a terrific mission statement for the FHA. We should allow the private sector to handle as much of the market as it can and the FHA should fill the niches.

The problem for the FHA, though, is that more and more of these niches are already being filled by the private mortgage insurers and also conventional lenders.

Therefore, we have to really, I think, reassess whether we need an FHA at all.

Now, let me basically say that I think there are about three reasons why the FHA is no longer necessary. And this gets mainly to the area of low-income.

Because the real issue here is do we need an FHA to handle low-income and minority communities, because I think everyone would agree now that, today, the middle-income homeowners and high-income homeowners are well served by the private sector.

I would make three responses to those who say that FHA has to be retained for the low-income markets.

The first is that the FHA increasingly is not serving low-income markets. There was a study that was done earlier this year by the Federal Reserve Bank that I could get for you, Senator, that shows that only 18 percent, less than one in five FHA loans were in low- and moderate-income census tracks.

That's an amazing statistic. Less than 1 in 5 is going to areas that are low-income.

Interestingly enough, we are working with a bunch of mayors to put together a contract with America's cities, a Federal contract with the cities. What can the Federal Government do to help cities?

We brought in about 8 to 10 mayors about a month ago. We were talking about what Federal policies help cities and what Federal policies hurt cities.

I was amazed to see that many of the mayors said, one of the policies that really hurts cities is the Federal Housing Administration. That seemed curious to me because is an agency that's supposed to be insuring mortgages in inner cities.

What they basically said is, no, that's not what the FHA is doing. The main thing that it's doing is, if you look at the 1 in 5 figure, what it means is it's going into inner cities and it's finding inner city residents who may be of moderate-income and it's telling them to go out to the suburbs and buy houses.

That's primarily why you've only got 1 out of the 5, even though it's serving low-income residents, I mean low-income people, it's not serving low-income communities.

A good example, by the way, of this——

Senator MACK. Say that to me again.

Mr. MOORE. If you look back at what Mr. Retsinas is saying about the extent to which the FHA is serving lower income people, that may be the case, that it's targeted towards low-income people. What I'm saying is it may be targeted to those people.

Those people aren't buying homes in the cities. They're taking people who live in cities now and they're saying, go buy a house in the suburbs.

That's, I think, what that Federal Reserve study shows. A good example, by the way, of the way that the private mortgage insurers can handle this market and the FHA doesn't is that a couple of years ago there was a study done on south central LA asking, where do these mortgages come from? Who made these mortgages and who insured these mortgages in south central, which is obviously one of the worst areas of the United States in terms of income.

What they found was that 90 percent of the mortgages were not FHA. They were either private mortgages or conventional loans.

And so, again, there's an example of where FHA, I don't think, is serving this market.

The second point that I would make is that the private mortgage insurance industry is increasingly servicing this market.

You talked earlier about this idea, but I'd bring to your attention this article that as just published in Mortgage Banking, which says, "How Big Can the Affordable Market Get?"

And the whole purpose of this article and the whole theme of it is the extent to which private insurers, mortgage bankers and so forth, are getting into the affordable housing market.

This, they argue, is the biggest area of growth in the housing market today, is affordable housing market, and therefore, they're making the case that Fannie Mae, for example, is developing new products to bring these houses to market. So are the PMI's and so forth.

In fact, last year, just to give you an example, General Electric launched about $1.7 billion of mortgage insurance in the affordable market.

The third point that I would make is that the FHA increasingly is actually doing harm to low-income areas. And the reason for this, and this was the point that, for example, Mayor Norquist was making to us when we talked to him about the FHA, is what FHA, to the extent that it does serve inner cities, one of the things that it does, because it makes very risky loans, is that you can go to a lot of areas—for example, in the city that I'm from, Chicago—and you can go through low-income neighborhoods in Chicago and what you're going to find is a lot of boarded-up houses.

Who made those loans? Mainly, it was the FHA.

The problem is that if you talk to some low-income housing advocates, which we have done, you're finding that a lot of them are saying the number one problem in terms of revitalizing low-income areas today is the FHA.

And the reason is that the FHA increasingly is trying to essentially make people take out mortgages that they can't afford. And this is a really important point because——

Senator MACK. Wait a minute. Say that to me again.

The FHA is making people take out——

Mr. MOORE. OK. I'm sorry. I didn't say that very well.

What I mean to say is that the FHA does not serve people when it entices them to take out loans that are beyond their means of repaying them.

Essentially, that is what is increasingly happening with respect to the FHA.

For example, over the last 10 years, there are 750,000 defaults on FHA loans. Those people who are defaulting on those loans are not being served by the FHA.

In other words, just because the FHA is giving a loan or insuring a loan to someone who is low-income, doesn't mean that they're doing a service to them because there's something worse than denying a person a loan. And that is enticing them to make a loan that they can't afford to repay.

That's, I think, one of the real problems with the FHA.

Let me just conclude, then, because I know I've used my time, by saying that if we can't essentially privatize FHA, then I think there are ways that you should really look at tightening the screws and making sure that better loans are made by the FHA and that the taxpayers' interests are being protected. And those are as follows.

First, I think the idea of less than 2 percent downpayment loans is just a recipe for disaster. The FHA should require about 5 percent downpayment on all the loans that it launches.

Second of all, there is no possible rationale for the 100 percent guarantee on FHA loans. FHA is the only institution that makes 100 percent guarantees.

Even the VA, for example, does not make 100 percent guarantees. What we should do, basically, is say, look, we will guarantee the first 20 percent. But the lender has to take some of the risk because the problem is when the FHA is guaranteeing 100 percent, that means that neither the realtor nor the mortgage bankers who make the loan have any incentive to make sure that this is going to be a good loan because if it goes bad, then the Federal Government picks up the entire tab.

Third, I would argue that there is no rationale whatsoever—if the mission of the FHA is to promote home ownership, then why is it that last year, 30 percent of FHA's business was refinancings?

Refinancings do not promote home ownership because you're talking about somebody who's already in a house.

And finally——

Senator MACK. Again, that 30 percent figure is based on?

Mr. MOORE. Last year's.

Senator MACK. Single-family?

Mr. MOORE. Yes. And the final point that I would make is that it makes sense to me again if we're going to target FHA to low-income and moderate income homeowners, that we should lower the threshold in terms of, lower that threshold from about $150,000 down to about $100,000, so that we are targeting this program to the one area where FHA may still have a mission.

Thank you, Senator.

Senator MACK. Thank you, Mr. Moore.

Mr. G. Richard Dunnells.

STATEMENT OF G. RICHARD DUNNELLS, ESQ., HOLLAND & KNIGHT, WASHINGTON, DC

Mr. DUNNELLS. Thank you, Mr. Chairman.

Being bracketed between Secretary Retsinas and Mr.

Moore makes me feel somewhat akin to the sparrow who flew into the badminton game.

[Laughter.]

The comments and my testimony, by the way, I am a private practicing attorney here in Washington. These are my own views, by the way, and I'm not representing the interests of any party or agency or entity.

Let me speak to the central purpose of this hearing, as I understand it. And that is to speak to the appropriate role or mission of FHA. Because I think, from what I'm hearing and sensing in the

dialogue, I don't think anybody is talking about totally extinguishing or abolishing FHA.

So I think the appropriate roles, and I applaud you for undertaking this inquiry, is on the mission, the appropriate mission for FHA and what is the appropriate vehicle, structure.

Should it be privatized? Should you try to fix the organization in place or come on with a new Government-controlled corporation?

When I tried to describe our National housing policy to people, I end up talking about interests and needs because that's the only dialogue that makes any sense to me.

In trying to articulate what the mission of FHA should be on a going-forward basis, I try to focus on needs and national interests. And here's where I come down.

In my perspective, we've got a society where we are seeing the escalation and polarization in age, economics, race, ethnic, you name it. We've got cities in decline. We've got neighborhoods in decline. We have family structures being fragmented.

There is simply no question that the supply of affordable housing is in very, very short supply for people that don't have the economic means to reach market-rate housing.

I think I should pause now and say that I'm going to address myself almost exclusively to the FHA multifamily residential programs and the health facility programs. I'm going to comment very briefly on the FHA single-family programs and the future, but I'm going to principally talk to multifamily and health care facilities because that's where my experience is.

So when I talk about the declines and problems in our society, I'm focused on interest groups that are not, in my judgment, being served and will not be served by other credit sources—private, public, and our GSE's, Fannie Mae and Freddie Mac.

In fact, it's my experience—and by the way, I worked with Fannie Mae and Freddie Mac and State and local housing agencies as well as FHA—the amount of affordable housing that's been developed in this country at present and over recent years, Senator, it's peanuts. It's peanuts.

Anybody that thinks——

Senator MACK. It might be helpful to, if you talk about affordable housing, to give us a sense of how you define it.

Mr. DUNNELLS. My definition of affordable housing is either new construction or the rehabilitation of multifamily housing that is serving families or individuals whose incomes are below 80 percent of median-income.

What I'm really focused on are persons whose incomes are below 50 percent of median income. But that's basically the range——

Senator MACK. You're talking again multifamily.

Mr. DUNNELLS. Yes, sir. Yes, sir. Again, I'm addressing principally multifamily and health care facilities.

I would have to say that if people agree that there is a need to provide affordable rental housing, in my view, you are not going to get private mortgage credit sources, Fannie Mae, Freddie Mac, or the State or local housing agency to meet this need standing alone. They're going to need something more to meet these niche or targeted needs in our society.

Again, I'm talking to low-income families. I'm talking to elderly. And I'm talking to special needs persons and renters.

I hope I'm making myself clear in terms of the focus.

By the way, when it comes to the health care facilities, and I think your question about hospitals is interesting. A lot of people don't realize the scope of the FHA health facility programs.

It's my experience that there are a number of health care facilities where private-sector financing simply isn't available or it's not available on economic terms.

We hear a lot about the conduit programs for financing health care facilities, particularly in your State. Those conduit programs are only interested in the high-end projects, the cream.

When you talk about financing a nursing home in Boseman, MT, forget it. Unless you've got FHA, you are not going to get a nursing home in Boseman, MT. Simple as that.

By the way, Nic Retsinas's comments about——

Senator MACK. Again, the reason for that, you say, is Boseman, MT, the financial structure of the community or the project that's put together just won't entice private financing?

Mr. DUNNELLS. You simply will not find lending sources that will finance that type of facility in that type of community.

I don't mean to single out Boseman, by the way.

Senator MACK. Yes. Fine.

Mr. DUNNELLS. Or the proposed financing is really uneconomic. It simply doesn't make sense to the developer from the standpoint of the amount of equity, the loan-to-value ratios, et cetera.

Part of this has to do with considerable apprehension about our National health care debate and the support mechanisms to basically support those types of facilities.

Senator MACK. But, again, I hate to kind of get stuck into this.

Mr. DUNNELLS. No, it's your hearing.

Senator MACK. It interests me, having made that statement, that we would encourage FHA to make loans under those conditions.

Mr. DUNNELLS. Senator, my whole theory about FHA is FHA ought to meet needs when the private sector will not or cannot respond to that need.

That is my whole approach to dealing with FHA. And perhaps I shouldn't have burdened you with my example of Boseman. But that's been my experience in looking at health care financing nationwide.

Senator MACK. You were going to make a comment about what Nic Retsinas had said.

Mr. DUNNELLS. Well, what he had said is true. When you talk to lenders and you approach lenders with respect to health care facilities, they are very concerned about the flow of Federal health care funds to these types of entities.

I have got some people out on the west coast that, they're getting out of the business because they're so apprehensive about the future of those flows.

Let me see if I can economize on my time and stay with the basics, and that is mission, mission and need.

Again, my reasons for wishing to preserve a multifamily FHA, multifamily residential and health care facility programs, I hon-

estly believe that there are needs and markets that are not met and will not be met by the private sector or your GSE's.

I have got a profound respect for Fannie Mae and Freddie Mac. But they have not been in this market. They do not finance the development or substantial rehabilitation of affordable housing. And anybody that thinks differently really ought to pay attention to what in fact Fannie Mae and Freddie Mac are all about.

To sum up on the point of need, it's my view that there really is no private or public sector equivalent to FHA when it comes to meeting these targeted niche needs with respect to multifamily housing.

Now, to get down to the real specifics about role or mission, I would try to be responsive to the question that you asked Nic Retsinas with maybe fewer words.

In my view, the appropriate role of FHA in multifamily ought to be, first and foremost, the provider of credit enhancement, private and public mortgage credit providers. That ought to be the role, always in partnership with private-sector or public entities, State or local entities.

Not doing the financing themselves, but always in partnership.

I would get the FHA out of the subsidy business, project-based or tenant-based. It is an inappropriate role, in my view, for FHA to perform.

One might ask, well, how can FHA provide a role in supporting affordable housing for lower-income families or for special needs families without getting involved in the subsidy business?

The answer is very simple. You have other agencies—Federal, State, and local, who can provide those subsidies or income supports for those types of consumers.

So what I see, and in my view, what you ought to have is an FHA that is a provider of mortgage insurance and credit enhancement and leave it to other agencies of Government, and particularly local and State agencies of Government, to deal with the incomes equation of needy renters.

That is about as succinct as I can get with respect to the role of FHA or the appropriate mission of FHA when it comes to multifamily.

Again, on the health care facilities, I don't want to take up a lot of time——

Senator MACK. I've interrupted you several times. You go right ahead and finish your statement.

Mr. DUNNELLS. I can sum up fairly quickly.

But in that basic role of being the provider of mortgage credit and credit enhancement, I also believe that you need to leave with FHA, multifamily, the ability and the capacity to underwrite on a loan-by-loan basis.

Having said that, I think there ought to be a lot more attention and a lot more effort by FHA to get into partnerships with private and local entities, Fannie Mae, Freddie Mac, on programs such as risk-sharing, reinsurance, top loss insurance, things like that.

In other words, dropping FHA more from the retail portion of the multifamily market more into the wholesale, i.e., as a support mechanism for other private and local and State entities.

So I really would encourage, and I know that Nic Retsinas wants to move in that direction and I think that is the appropriate role for FHA.

Last but certainly not least, whenever you're talking about FHA multifamily, you are talking about a huge investment in our present portfolio of multifamily and health care facilities. We've got close to 15,000 multifamily insured projects out there. We've got about 2,200 HUD-held. You've got about 950 health insurance and 5,000 202 elderly and handicapped.

That is a huge investment and a huge exposure. Again, I'm only talking about multifamily right now, not single-family.

To try to conclude, a couple of comments on structure.

I have thought a lot about the proposals to privatize FHA. I have come, in my own view, that privatization really just doesn't make a lot of sense. And the reason I say that is this.

It seems to me that, for the most part, these FHA multifamily programs are really not in competition with the private sector.

Second, it's my view that you need an FHA multifamily to really meet and serve these various national interests and national leads. I've only alluded to the role that FHA plays in providing mortgage credit supply. There are other roles.

The demonstration of new techniques and new mortgage instruments, the standardization, all these other ancillary roles—I think they're important.

But I just keep coming back to the question, why privatize FHA when you've got a proposal and an opportunity on the table to return FHA to a self-sustaining, effective vehicle to deliver mortgage credit insurance and credit enhancement to the private sector and to meet these national needs?

I'm not hearing Democrats and Republicans arguing about the need for change within FHA or the direction of FHA. But it seems to me that we've got an opportunity to maybe in part fix something which is broke.

By the way, let me just give a comment, too, about the need for this restructuring.

I sincerely believe that FHA, as it presently is configured, is broken. The programs are too complicated. They're overregulated. You've got this intertwining of subsidy programs and mortgage insurance programs.

But what concerns me most about the FHA today is the organization and the people and the attitudes.

FHA lacks professionalism. It lacks discipline. It lacks basic pride and respect and loyalty among its employees for the organization itself.

I don't criticize people like Nic Retsinas or Helen Dunlap, who was sitting behind him. These are bright, dedicated people. But they're working within a dysfunctional organization and they're working against regulatory and bureaucratic constraints which kills the best of incentives.

That's a big problem in FHA. I am sad to say, I don't think that can be fixed in the present configuration.

A quick note on single-family and then I'll pack it in.

I don't have quite the same feelings, Senator, about the role and mission of FHA single-family that I do for multifamily. I think that

Mr. Moore makes, particularly with the overlap of FHA single-family and the PMI's has a lot of merit. I do see a lot of overlap.

I don't, however, feel qualified to comment on the PMI's, the private mortgage insurers proposal that FHA single-family be limited, really, to first-time homebuyers and to low-income home purchasers.

I've been around the PMI's for a long time. They talk a great game. But when mortgage markets head south, risks go up, and profit margins decrease, we've seen the flights of PMI's from various markets.

So I think the PMI proposals for targeting, my instinct is they sound like a bad idea. And I read in that proposal to target FHA single-family to first-time homebuyers and low-income, to basically simply be creating another low-income housing agency with higher risks, higher costs, and higher failure rates.

I don't have much more to add on the single-family. But one thing I would say. I think whatever comes out of the legislation, there ought to be a clear and unequivocal message from the Congress that the Congress wants FHA single-family to move out of the retail segment or component of the single-family mortgage market and take on more the role of the reinsurer, the coinsurer.

In other words, an undergirding type of role as opposed to being out in front and basically what I would call the retail segment of the FHA single-family programs.

I think that message has got to be delivered, delivered and delivered. And I think it's the appropriate message to deliver to single-family.

Senator MACK. Very good. I appreciate the testimony from both of you this morning. I don't think we'll keep this going too much longer, but I do want to raise some additional questions.

I might start with this concept of the targeting.

I don't remember, Mr. Moore, whether you focused in on the targeting issue, but let me just pick it up with Mr.

Dunnells and then see what kind of reaction you have.

I go back to this comment that Mayor Steve Bartlett made to me about maybe we ought to encourage FHA to do more in the inner-city, notwithstanding——

Mr. MOORE. He's one of the mayors, by the way, we've been working with.

Senator MACK. OK. In essence, that would really be targeting both geographically where credit is needed, capital is needed, and also, I would assume also would reach a good portion of low-income people, or a good number of low-income people.

But I think what you're saying is if we get too specific or too narrow in our targeting, we set up a situation where we just create, I would assume, the potential for huge losses and we eliminate any possibility of keeping good loans in the portfolio that, in essence, acts as a subsidy for the bad loans.

Is that a fair way of saying it and do you agree with that?

Mr. DUNNELLS. Well, I think that, yes. I would say that if you want FHA to become nothing more than another low-rent public housing agency, national, regional or local, then target them. But I don't think that's the appropriate role for FHA.

What I would much prefer to see, again, are Federal, State or local agencies address the incomes need of the consumer, i.e., the tenants or the special needs people, and have FHA over here as a credit source to finance that development or that transaction or that activity.

I think when you have FHA crossing the line and become an agency that is more concerned with the incomes problems of its tenants and its consumers, you're going to put FHA right back in the same box it got into back in the 1960's.

That's when FHA crossed the line. It was with the Great Society programs and the dependency on tax shelters first and then Section 8. That's when FHA lost its self-sufficiency, quite frankly.

What I'm saying, and I'm maybe not saying it very clearly, but I would try to have FHA as a self-sustaining, disciplined professional provider of credit and credit enhancement and then have other agencies and other resources address the incomes problem.

Senator MACK. Very good. Mr. Moore.

Mr. MOORE. Yes. I want to address that.

This cross-subsidy issue comes up a lot. In fact, whenever the issue of targeting is made, the mortgage bankers say, well, we can't do that because when we take in more high-income people, they cross-subsidize the lower-income people.

I think that that's a very dangerous argument and let me explain why.

First, just on a philosophical level, getting back to the question about what's the mission of FHA. I think that we should all agree that the mission of FHA is not to compete with a private-sector market. If the private-sector market is handling an area, then I think that we should get the FHA out of that area.

With respect to people of middle-income and high-income people, they are served by the private market. And I think it's offensive when the FHA says, we have to get into that.

Second of all, we should not be making bad loans to low-income people. That is, there should be no reason for a cross-subsidization. It does not serve anyone's interest. Most importantly, it does not serve low-income people's interests to put them into high risky loans that they can't repay.

You have some areas where the FHA is putting people into cities, where the default rates go 20, 25, even 30 percent.

Now, Senator, that does not serve a family's needs when we're enticing them into these very low downpayment loans and we have to then 2 years later chase them out of their house.

Third is that I think it's important to realize——

Senator MACK. So you think there's adequate evidence out there to indicate and support that position?

Mr. MOORE. I'm sorry? Which? The one about the——

Senator MACK. In essence, encouraging people to borrow, to purchase a home that they can't afford and that the default rates are higher.

Mr. MOORE. Yes. The default rates, for example, last year, for example, delinquency rates in the private sector went down. Last year, FHA's default rate was about twice as high, two to three times as high as it was for the private market.

So I think there is strong evidence, especially in a lot of inner cities where you do have delinquency rates on FHA properties of 25 to 30 percent.

Now, what I'm trying to say is, are they enticing them into these loans?

Well, the point is that they're making loans that—for example, if the private industry, if the private mortgage insurers tried to make some of these loans with 2 percent downpayment, 100 percent protection on the loan and so forth, the State regulators would close them down. They'd put them in jail.

You can't do that in the private sector. They would say, this is a very bad lending practice that you're engaging in.

So, I guess my point is that we should have the FHA engaging in sound lending practices because it's good for taxpayers and it's good for low-income people.

Senator MACK. I think you had a third point you wanted to make.

Mr. MOORE. The third point I was going to make was with respect to this cross-subsidization issue.

The most important thing on the soundness of a loan is not the income level of the homebuyer. It's the size of the downpayment. The downpayment is the whole ball game with respect to whether someone is going to default.

In many cases, the FHA is not cross-subsidizing. In other words, it would be better to make a loan, for some who is very low-income, a $40,000 loan with a 5 percent downpayment than for someone who makes $100,000 a year with a higher downpayment because the downpayment is the predictor of default rates, not the income level of the buyer.

Senator MACK. Both of you were here when Mr. Retsinas and I engaged in a series of questions. I was curious whether there were some areas that you wanted to respond to, either of you, about those questions, points you wanted to make with respect to that discussion.

Mr. DUNNELLS. I was intrigued, Senator. Maybe it's not fair to Nic Retsinas because they're still in the drawing board stages of the new corporation.

I think your forcing the proponents of the new corporation to factor clear mission objectives into their structuring is a very good idea.

To give you an example. I hope that they don't replicate this 80-plus field office structure they have in HUD today for the new FHA. That is just nuts.

What you ought to be doing is consolidating your staff, making the most of your professional resources, enhancing your underwriting and monitoring disciplines.

I think really pushing at that structure is a very good idea and that will touch on mission as well. No question about it.

Mr. MOORE. The only thing that struck me about the proposal is the extent to which the administration now is, I think, conceding that we need to do a much better job of targeting with respect to FHA.

Everyone is coming together on this issue that the FHA, I think, should be targeting its efforts more towards the low- and moderate-

income levels and not middle-income and higher-income homebuyers.

It's good to see people coalescing around that point.

Senator MACK. Mr. Dunnells, if I could, let me pose a question or two.

HUD proposes to establish public purpose performance requirements for the new Federal housing corporation, such as requiring a certain amount of the corporation's business to benefit homebuyers underserved by the conventional market or to benefit certain underserved geographic areas.

Do you agree with the establishment of such performance requirements?

Mr. DUNNELLS. That's like arguing against motherhood.

Senator MACK. I realize it's obvious.

Mr. DUNNELLS. I get kind of a bad glitch when I hear performance standards targeting to underserved. I'm beginning to read into that the same sort of problem that I was attempting to address earlier. And that is the blending and mixing of functions.

Again, not to repeat myself, but I really think FHA ought to have a credit enhancement mortgage insurance function over here and there ought to be other agencies that address incomes issues and incomes problems. So when you have performance standards that are directed to serving various segments of society—I guess I would have to say that I would like to see the performance standards and whether they take account of what I see as a separation of functions between FHA and other providers that will fully serve that particular segment.

I get a glitch when I hear performance standards stated that way.

Senator MACK. I really just have one last question and it's to both of you.

Do you believe it's possible to run an agency with a public purpose, social mission in a business-like manner and still meet the test of both social and fiscal responsibility?

In other words, does FHA want to do something that it is impossible to do?

Mr. DUNNELLS. I think you can't have it both ways. If you're going to have an economically self-sustaining organization, you've got to move it further away from the social purpose of the social welfare component.

If you're prepared to have that agency play and participate in that social service, social welfare, then understand it's going to lose money. It's going to take risk. And it's going to be something else than a self-sustaining corporate entity.

This is why—and I've been working in the private sector all my life, with the exception of 4 years at HUD. Every time I see the profit motive bump up against the public purpose motive, the public purpose motive loses.

Senator MACK. Well said.

Mr. MOORE. First of all, I agree with what you're saying. Also, I would simply say that, yes, there was an important social mission that FHA played for about 50 years. And I think we should applaud it and this is, what, its 60th birthday now. Maybe we should have a big birthday cake for it and start to privatize it now.

As we look forward to the 21st century and the affordable housing market is changing so rapidly in terms of, for example, what I was talking about earlier, the way the private insurers and the way that Fannie Mae and Freddie Mac and mortgage bankers are really seeing this as the growth potential in housing.

It strikes me that FHA is more and more using kind of a 1950's approach to 21st century kinds of housing needs.

Senator MACK. Let me just, I'm going to try to put together a thought here with respect to what you all have said, with this conflict between private profit motive and a social objective.

It almost seems like we would be better off if we accepted—let me back up.

Assuming that the Congress would conclude that it's in the country's best interest and the best interest of our society to enhance the potential for home ownership with low-income folks and families, and recognize that there's a cost to doing that, and not try to get it fuzzed up by cross-subsidies and having this institution create the impression that it is a privately-run, profit-motivated, market-driven institution, I think you're right. I think it is extremely difficult to do that.

The question really is is the Congress prepared to openly state, we're going to involve ourselves in the development of a program for the purpose of expanding home ownership in the country beyond the 65 or so percent where it is today, and we realize that there's a cost for that and we as a Nation are prepared to pay that cost.

I think that's a very straightforward question that ought to be posed to my colleagues and I think you all have been helpful in focusing me on that point this morning, and I thank you for doing that.

Again, I thank you for being here and I appreciate your interest and I appreciate the time that you've spent to provide us with your ideas.

Mr. MOORE. Thank you.

Mr. DUNNELLS. Thank you, Senator.

Senator MACK. The Subcommittee stands in recess.

[Whereupon, at 11:34 a.m., the Subcommittee was recessed.]

[Prepared statements and response to written questions for the record follow:]

TESTIMONY BEFORE THE SENATE SUBCOMMITTEE ON HOUSING OPPORTUNITY AND COMMUNITY DEVELOPMENT

May 4, 1995

By

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER
NICOLAS P. RETSINAS

I. Introduction

Thank you, Mr. Chairman, for the opportunity to discuss the mission of the Federal Housing Administration (FHA) and HUD's proposal to transform FHA's structure, products, and accountability.

After less than 1 year in office, as HUD approached the 60th Anniversary of FHA, the Secretary asked me to undertake a study designed to ascertain the mission of FHA and how it could be best organized to carry out that mission. With the assistance of Harvard's Joint Center for Housing Studies, I conducted eight forums around the country with FHA's program participants, partners, and customers, along with other housing experts and providers. Representatives from more than 150 groups participated. The Joint Center will be releasing a report summarizing these forums later this month.

Our inquiry had just concluded last winter when the President asked a number of agency heads to explain whether the mission of their agencies was still relevant in a time of diminishing resources and streamlining Government. When the Secretary presented his vision of the mission and future of FHA to the President, he had the benefit of having heard from across America that, while FHA has a continuing and vital role, it must be radically transformed if it is to carry out that mission in the modern world of housing finance.

This week, the Administration sent the Congress the American Community Partnership Act—which includes a charter for a new, wholly-owned Government corporation—the Federal Housing Corporation—to accomplish that transformation.

This morning, I would like to talk to you about HUD's proposal and some of the alternatives being suggested by others. But first, I think it would be helpful to briefly review the findings of our study of the mission and future of FHA.

II. The Future of FHA—Findings

A. FHA's 60-Year Record of Achievement

Congress created the Federal Housing Administration in 1934 to help the country get back on to the road to economic recovery. At the time, the housing industry was flat on its back. Two million construction workers had lost their jobs. For homebuyers seeking mortgages, the terms were terrible. Loans were limited to 50 percent of value, spread over 3- to 5-year terms, ending in a balloon payment. In those days, America was primarily a Nation of renters. Only 4 in 10 households owned homes.

In the 60 years since FHA came on the scene, a lot has changed. Thanks to the mortgage insurance products FHA helped to pioneer (like the low downpayment, self-amortizing, long-term mortgage), our Nation's home ownership rate now exceeds 64 percent. Americans are arguably the best housed people in the world. FHA contributed substantially to that achievement.

During the 1940's, FHA programs helped to finance military housing and then homes for returning veterans and their families. In the 1950's, 1960's, and 1970's, FHA stimulated production of millions of units of privately-owned apartments for elderly, handicapped, and lower-income Americans. When soaring inflation and energy costs in the 1970's threatened the economic viability of thousands of private apartment buildings, FHA's emergency financing kept cash-strapped properties afloat. When a deep recession prompted private mortgage insurers to pulled out of oil producing States in the 1980's, FHA moved in to stabilize falling home prices and ensure purchasers could find financing for homes they wanted to buy.

Today, FHA is a $380 billion dollar insurance company—with more than 40 insurance programs—that has successfully opened the door to home ownership and affordable rents for millions of American families and seniors for more than 60 years. Without costing the American taxpayer a single dime, FHA has made home ownership possible for more than 23 million households, whom the private sector could not serve. In addition, through FHA insurance, 4.5 million rental units have been financed and more than 312,000 beds in community hospitals, nursing homes, and other assisted living facilities have been created.

Those helped by FHA today are Americans and communities that are not adequately served by the private market.

- FHA insured 1.34 million single-family mortgages in FY 1994, a 42 percent increase from the previous year, and the second highest year on record. 450,000 of these, 67 percent of the purchase money mortgages, were first-time homebuyers, more first-time homebuyers than both Fannie Mae and Freddie Mac combined.
- Nearly one-third of all moderate-income homebuyers rely on FHA mortgage insurance to enable them to purchase a home. Nationwide, the average income of families securing FHA loans in 1992 was $37,000, compared to $55,000 for loans with conventional financing.

- Forty-seven percent of FHA mortgages were written on homes valued at less than $70,000 compared to less than 22 percent of privately insured mortgages, in the last quarter of FY 1993.
- Almost 30 percent of FHA-insured loans in metropolitan areas benefited underserved census tracts, compared to only 15 percent of conventional, conforming mortgages.
- Forty-five percent of *all* home mortgage lending to African-Americans and Hispanic Americans (in metropolitan areas) is FHA-insured.

B. A Revolution in Housing Finance

FHA was once the leader in the development of the Nation's system of housing finance. In recent years, new lenders have joined savings and loans as major residential mortgage lenders, the private mortgage insurance industry has recovered strongly from earlier setbacks, technology has dramatically shrunk the time it takes to originate loans and transfer them to investors, and the secondary market—including the Government-Sponsored Housing Enterprises (GSE's)—has dramatically improved the liquidity of the home mortgage finance system. Private sector market participants, together with the Government housing finance institutions—FHA, Ginnie Mae, the Federal Home Loan Banks, the Federal Reserve Banks, the Federal Deposit Insurance Corporation—create a mortgage finance capital delivery system that is, without a doubt, the most sophisticated in the world.

C. Unmet Housing Needs

Notwithstanding the achievements of the public and private sectors, there are many housing needs in this country that are not being met. At the FHA Forums throughout the country, we heard repeatedly that the Federal Government must not abandon its historic role of helping the private sector to meet these unmet needs.

Although the system for delivering capital to single-family housing is extremely efficient, it does not reach all the creditworthy Americans who could afford to own their own homes. There are potential first-time homebuyers, young or low- and moderate-income families, racial minorities and immigrants, who continue to face barriers to home ownership. The national home ownership rate has declined by 1.5 percent since 1980. This overall decline has been much more dramatic among young families and minorities. While home ownership trends have improved since 1993, the levels are still well below historic peaks.

President Clinton has called for reversing the 1980's downward trend by expanding home ownership in America to all-time high levels by the end of the century, generating up to 8 **million additional homeowners** between the beginning of 1995 and the end of the year 2000. This **National Homeownership Strategy** will accomplish the ambitious goal through an unprecedented nationwide public-private partnership involving leading organizations from the housing industry, State and local government, nonprofit groups, financial institutions, and Federal agencies. FHA is an important partner in this national effort, though it must be transformed if it is to contribute significantly to expanding home ownership to new heights.

The system for delivering capital for rental housing is not nearly as well-developed as it is for home ownership. The system works even less well for affordable rental housing. The Nation's principle supply of affordable rental housing is found in its older housing stock, often in smaller properties owned and managed by individuals and small businesses. The private market has few tools to meet the large capital needs of this housing stock and the supply is dwindling. Harvard's Joint Center estimates a national shortage of 4 million affordable housing units, and HUD counts more than 5.6 million households living in substandard dwellings and paying more than 50 percent of income for housing.

Low- and moderate-income families, many of them first generation Americans, just starting out in life, are looking to climb the ladder of economic opportunity by renting an apartment in a decent, stable neighborhood with good schools, and close to jobs and transportation. Working class families, the elderly, and disabled persons, in many cities find the supply of good rental housing at affordable rents to be increasingly scarce.

Although securitization and other secondary market mechanisms have begun to bring more capital to rental housing, these tools are limited and require large volumes and standardization—requirements that are incompatible with typical community reinvestment lending, loans for smaller properties, and affordable projects requiring multiple layers of local subsidy and other financing sources. Even the capital available for market-rate rental housing tends to be diverted cyclically to alternative investments in pursuit of higher yields and lower perceived risks.

D. THE CONTINUING MISSION OF FHA

Since that National Housing Act of 1949, it has been national policy that the Government's role is not to compete with the private sector but to meet needs the private sector cannot serve, while expanding the private sector's capacity to meet more and more of the need on its own. During the last 60 years, this has been FHA's primary purpose—to expand home ownership and rental housing opportunities for families not adequately served by the private mortgage markets, while demonstrating opportunities for the private sector to do more. Given the continuing unmet needs, this mission remains relevant today and is accomplished in five ways:

1. FHA expands access to capital to creditworthy people, neighborhoods, and markets that the private sector determines are too risky for them to profitably serve. For example, FHA borrowers have lower-median incomes, lower mortgage amounts, lower downpayments and fewer reserves than to conventional borrowers.

2. FHA pioneers and demonstrates untested products that the private sector will not offer because risk is uncertain. Long-term, amortizing, low-downpayment mortgages—the staple of today's mortgage finance system—were an FHA creation. More recently, FHA has pioneered the home equity conversion mortgage to help house-rich but cash poor seniors stay in their homes.

3. FHA provides access to capital and stability in mortgage markets during economic downturns when the private sector is driven to withdraw. For example, when the 1980's recession hit the oil patch States, private mortgage insurers left, some only paying 40 cents on the dollar for their obligations. FHA paid every claim and kept the flow of capital, heading off even more precipitous declines in property values and destruction of homeowners' savings.

4. FHA spreads risk across a diverse portfolio of products and borrowers. FHA's portfolio includes segments that, although they are not be sufficiently profitable to attract most private insurers, allow FHA to serve other borrowers who, as a class, cannot be served on a self-sustaining basis. For example, if 5 out of 100 borrowers with certain characteristics will default, and their premiums will support only 4 claims, the private sector will serve none of those 100 borrowers. FHA's ability to cross-subsidize allows 95 new homeowners to share in the American dream.

5. FHA's presence provides an alternative in the market prompting private actors to compete more efficiently in lower-profit market segments, making more capital available for consumers and lowering home ownership costs.

Why can FHA serve this mission when the private sector cannot? The answer lies in the unique abilities of the Federal Government. FHA's government backing provides the market with additional assurance that it will be able to pay insurance claims. Private insurers, on the other hand, must earn a profit sufficient to set aside the high levels of capital required by State regulators and their shareholders to provide adequate assurance of the ability to pay claims and earn profits for shareholders. (In recent years, some PMI's had earned returns on equity of 18 percent.) This cost advantage, coupled with FHA's higher premiums, allows it to support a higher level of losses and thus serve untested or higher-risk borrowers, at no cost to the taxpayer.

E. CHALLENGES FACING TODAY'S FHA

Although FHA continues to serve important needs, the institution faces enormous challenges. You would be hard pressed to find anyone who does business with FHA arguing against reinventing the agency. Like many Government organizations, our processes are too cumbersome and our bureaucratic structure needs updating to enable us to serve our mission in a world of modern technology and fast-moving capital markets.

FHA needs greater product design flexibility to perform its role as an **Innovator** pioneering new mortgage insurance products, processes, and partnerships. For example, we could provide insurance for lease-purchase programs that would enable many low- and moderate-income families to own a home by using their monthly rent to save for a downpayment. Yet we cannot experiment with such a program without legislative authorization. In the time it takes to enact a new statute, market changes may cause the opportunity to be lost.

FHA also needs greater flexibility to address longstanding management problems. Auditors have repeatedly pointed to four material weaknesses that HUD has struggled to remedy for many years:

- The need to address weaknesses caused by lack of staff and administrative resources. Resource constraints have prevented FHA from devoting adequate attention to loss mitigation, properly managing troubled assets, and quickly implementing new automated systems.

- The need for more emphasis on early warning and loss prevention. Information systems, staff training, and attention must be devoted to identify and react to troubled mortgages before they default.
- The need to resolve defaulted notes and HUD-owned properties. The growing HUD-held and HUD-owned portfolio drains staff resources and takes away from adequate monitoring of FHA's large portfolio of insurance-in-force.
- The need to improve automated systems to increase the reliability and utility of information gathered to support management decisionmaking.

In June 1994, Price Waterhouse noted that HUD plans represent a "comprehensive and serious effort . . . to address problems that have plagued FHA for many years." They expressed deep concern, howevr, about HUD's ability to follow through on those plans in the face of budgetary and legislative constraints. We have made some real progress in addressing these concerns, but we too share the auditors' belief that the current structure of FHA will frustrate our ability to make the changes needed to restore the public's confidence in FHA and to make it even more effective at meeting the Nation's unmet housing needs.

F. PUTTING FHA BACK IN BUSINESS

Our commitment to change can be measured by the progress made in the last two years. The Department has made tremendous strides in putting FHA back in business for families and communities:

- According to our independent auditor, Price Waterhouse, the Mutual Mortgage Insurance Fund achieved the capital ratio mandated by Congress for Fiscal Year 1993. All evidence suggests that the MMI Fund continues to strengthen.
- Fiscal Year 1994 was the second best year for single-family business in the 60-year history of FHA, insuring more than 1.34 million loans.
- Recently, FHA conducted several successful mortgage sales, reducing our initial multifamily inventory by 20 percent, reducing our workload, and reducing the risk exposure of the multifamily insurance funds. This past March, the Department auctioned $1 billion in multifamily mortgages, generating proceeds of approximately $710 million. These sales are part of a 2-year strategy to sell single and multifamily mortgages that have been assigned to the agency. These sales, we project, will generate substantial net revenue to the Government.
- We reduced the HUD-held multifamily inventory by 34 percent, selling one property every 2 days. We reduced the Single Family inventory to the lowest year-end total in the last 9 years.
- We established a prototype single-family development processing center in Denver that drastically cut loan processing time from weeks down to an average of 2 days.
- We modernized and improved FHA's underwriting guidelines to reach out more effectively to underserved populations and areas.
- We lowered our single-family mortgage insurance premiums by 25 percent.
- FHA has successfully pioneered a new product, insuring more than 10,000 reverse-annuity mortgage since the program's inception, enabling seniors who are house-rich but cash-poor, to have the security of a steady income stream to pay,for health care and other necessities, while maintaining their financial independence.

These accomplishments put us on the right track, but more dramatic change is necessary if FHA is to perform its modern mission in today's environment.

The most important conclusion from the forums is that FHA needs to be able to operate as a business with a public purpose. That means it needs to be able to form partnerships with public and private entities to create new ways of reaching untapped markets and delivering its products more effectively; it needs flexibility in the design of its products, allocation of its resources, and acquisition of needed systems, skills, and expertise; and it needs to demonstrate to the Congress and the public that it can be held accountable for how well it serves its public purpose mission and manages its financial obligations. These conclusions lead us to propose that FHA be transformed into a wholly owned government corporation.[1]

III. The New Federal Housing Corporation

The new Federal Housing Corporation (FHC) would be a self-sustaining financial institution with clear accountability for performance and results, both in serving public purposes and maintaining financial safety and soundness. This new Corporation can best be described in three parts: Business products, partnerships, and plan-

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[1]The National Academy of Public Administration recommended FHA be restructured as a Government corporation in its July, 1994 report to the Congress *Renewing HUD: A Long-Term Agenda for Effective Performance.*

ning; performance requirements and accountability; and management and organizational structure.

A. Business Products, Partnerships, and Planning

The Corporation will provide direct, 100 percent mortgage insurance, just as FHA does today. However, the Corporation will develop an annual business plan reflecting a variety of business products designed to best serve its public purposes. The annual business planning process will enable the Corporation to adjust product mix, pricing, and design as market needs change, without the delay inherent in seeking new authority.

The Corporation will engage in single-family, multifamily, and health care financing business. Over time, more of the Corporation's focus will shift to risk-sharing endeavors, pairing the FHC's federally backed credit enhancement product with the resources of private and public entities that have local market knowledge, technology, and financial expertise. These partners will share risk and perform much of the processing and servicing of loans. Risk-sharing partners will be required to demonstrate their creditworthiness in order to participate. Of course, the Corporation will continue to provide FHA's traditional 100 percent, single-family insurance product, as well. The precise product mix will depend upon market needs and the ability of the FHC to meet safety and soundness and programmatic performance requirements.

Additionally, the Corporation will engage in other types of partnerships with private and public entities, for various business functions. For example, the Corporation intends to conduct some of its asset management and disposition activities with the help of skilled private and public entities. Additionally, the Corporation will rely on local and State partners to assist in identifying underserved markets and to provide additional, technical support.

The new business of the Corporation will be limited in two ways. First, no new business under the new charter may be undertaken until the Secretary approves a business plan and the Corporation's safety and soundness regulator, the OFHEO Director, determines that it is consistent with meeting capital standards. Each year, the Corporation's business plan will be subjected to the same review.

Second, the Corporation's single-family products will be subject to the same maximum mortgage limits that are in effect for FHA today—a ceiling, equal to 75 percent, and a floor, equal to 38 percent, of the conforming loan limit. Moreover, the Corporation will be subject to an aggregate 5-year business volume limitation, equal to five times FHA's total commitments executed in 1994—for single-family, multifamily, and health care financing combined—or $518.35 billion. These restrictions should provide assurance that the Corporation will not unnecessarily compete with the private sector.

The FHC will be fully self-sustaining in connection with new business undertaken under new authorities. However, the Corporation's activities will continue to be reflected in the Federal budget and subject to the Federal Credit Reform Act. After its initial capitalization, the Corporation will generate all of the revenues needed to sustain its operations and maintain adequate capital reserves.

The new Corporation will be delegated authority from the Secretary to undertake certain business in connection with existing insurance funds. This delegation is twofold. First, it will permit the Corporation to undertake new business under existing authorities for an interim period, until the Corporation's new authorities are fully operational and prior to the repeal of Titles I and II of the National Housing Act, 5 years after the commencement of new authorities under the charter. Second, this delegation will permit the Corporation to undertake portfolio management and resolution activities in connection with outstanding FHA insurance-in-force. The delegation of these authorities to the new, better skilled, more flexible Corporation will ensure that FHA's losses will be minimized and returns to the taxpayer will be maximized.

B. Performance Requirements and Accountability

The self-sustaining FHC will be more accountable to Congress and the taxpayer than FHA ever could be. This accountability is possible because the charter Act establishes a "bottom line" for performance, yet allows the Corporation to determine the best way to meet or exceed those goals. Specifically, the FHC charter measures two types of performance: Public purposes and safety and soundness.

The public purpose performance requirements ensure that the Corporation will always serve the market for which it was chartered: Those vulnerable American families, communities, and market niches which are or have been historically underserved by the private mortgage markets. Specifically, the Corporation will be subject

to four public purpose performance requirements which will ensure that a portion of its business serves the underserved. These requirements include:

- **Underserved Homebuyers:** Which will measure the extent to which the Corporation benefits, for example, first-time homebuyers and families typically underserved by the private mortgage markets, including minorities, immigrants, and young households lacking savings.
- **Underserved Areas:** Which will measure the extent to which the Corporation benefits underserved portions of central cities, suburban and rural areas, including low-income and minority census tracts.
- **Underserved Rental Markets and Related Community Needs:** Which will measure the extent to which the Corporation's business benefits rental markets and health care facility financing needs underserved by the private mortgage markets.
- **Low- and Moderate-Income Families:** Which will measure the extent to which the Corporation benefits families who earn income that is at or below the median income for an area.

During an interim period, the Corporation will be required to produce results which at least equal FHA's performance in 1994, with respect to each requirement. For both the interim and the permanent requirements, the Secretary will monitor the public purpose performance of the Corporation, in much the same way that the Secretary monitors the affordable housing goals which were statutorily imposed upon the Government-Sponsored Housing Enterprises (GSE's)—Fannie Mae and Freddie Mac—in 1992.

In another parallel to the GSE's, the Corporation will be subject to a safety and soundness regulator, the Director of the Office of Federal Housing Enterprise Oversight ("OFHEO"). OFHEO will develop a risk-based model to assess the adequacy of the Corporation's capital. Moreover, as the safety and soundness regulator, the OFHEO Director must approve the Corporation's business plan prior to inception. In this manner, the Corporation will be doubly accountable: (1) it will be subject to a "backward looking" review of actuarial soundness; and (2) it must demonstrate, *before* new business plans may be implemented, that those plans will not threaten the Corporation's financial safety and soundness. Additionally, the risk-based capital standard will ensure that the Corporation is able to withstand an adverse economic scenario. This capital standard will be applied to the Corporation's business as a whole, permitting those lines of business that generate more revenue to support less profitable lines of business. If the Corporation's capital level fell to unacceptable levels, the OFHEO Director would be required to make recommendations for restoring capital adequacy to the CEO and the Secretary and report its findings simultaneously to the Congress.

The FHC will be subject to additional oversight and reporting requirements, including: Audited financial statements; audits by the Comptroller General and the HUD Inspector General; the Secretary's annual report on public purpose performance; OFHEO's annual report on safety and soundness performance; and an annual business-type budget.

C. Management and Organizational Structure

The Corporation will be a wholly-owned Government corporation, subject to the requirements of the Government Corporation Control Act. That Act was passed by Congress in 1945 with the understanding that certain Government functions—most notably, those business-like activities with revenues and the potential to be self-sustaining—should operate with more flexibility, free from some of the prescriptive requirements imposed on other Government agencies.

The Federal Housing Corporation will be a Government corporation located within HUD, in much the same way the Government National Mortgage Association ("Ginnie Mae") is located, and operates a sophisticated financial business, within HUD. The Secretary of HUD will have general oversight over the Corporation. The Corporation will be managed by a Chief Executive Officer, appointed by the President, by and with the advice and consent of the Senate.

The Corporation's structure is designed to provide the flexibility needed to operate in sophisticated housing finance markets. For example, the Corporation will have certain exemptions from civil service pay and classification requirements—similar to the exemptions the banking regulatory agencies have—to enable the Corporation to attract and hire qualified financial staff and other technical expertise. Like a business, the Corporation will develop its own personnel and procurement procedures, although personnel will continue to be Federal employees. The Corporation will ensure that, while suited to the particular financial and technical needs of the Corporation, procurement and personnel procedures will be fair and nondiscriminatory.

The Corporation's ability to procure expertise as needed will immediately address current weaknesses inherent in FHA's structure which, for example, have impeded its ability to manage and dispose of multifamily assets in a timely and cost-effective manner. As you may know, it took FHA 11 months to obtain a financial adviser, during which time interest rates rose. Although our first major sale of assigned notes last month was remarkably successful, the returns might have been greater and the cost of holding the assets lower if the sale had occurred a year earlier.

HUD's legislative proposal also contains modifications to the Ginnie Mae charter to make it easier for FHA and Ginnie Mae to operate more effectively as partners in the system for delivering capital to affordable housing. Ginnie Mae will continue to serve as the primary secondary market vehicle for mortgages with FHA credit enhancement. Ginnie Mae's charter will be modified to give it the same rulemaking, procurement, and personnel authorities as the FHC.

D. ROLE OF THE FHC IN MULTIFAMILY PORTFOLIO RESTRUCTURING

Finally, the new FHC will be capable of obtaining the specialized skills necessary to manage FHA's existing multifamily portfolio. In fiscal year 1993, FHA had to set aside a $10.3 billion loss reserve (down from $11.9 the previous year) to cover anticipated losses in connection with its outstanding multifamily insurance-in-force. To prevent all those losses from being realized, FHA needs staffing and procurement powers that will be available under the new FHC. Specifically, the new FHC would be able to manage the portfolio of multifamily properties owned and notes held by the Department, and restructure the debt on outstanding multifamily insurance-in-force. The process, referred to as "mark-to-market," will reduce the debt on insured multifamily properties to levels which can be supported by the market, ending the physical and financial decline of many of these properties, and once and for all, terminating the over-subsidization of certain properties, while protecting tenants and providing them with choice. Over the long term, this process will contain the inordinate costs of renewing Section 8 contracts which will begin expiring in this calendar year.

IV. The Alternatives

We certainly recognize that we are not the only ones thinking about the future of FHA. Other proposals have been discussed and I would like to share some preliminary reactions.

There are three basic arguments being made.

1. With the growing sophistication of the private sector and the introduction of the conventional, 3 percent downpayment loan, the private sector can now serve most of the need served by FHA. FHA, therefore, can be eliminated without any significant loss to the public interest.

2. FHA can be sold to the private sector who can accomplish its mission more efficiently.

3. FHA can be narrowly targeted to serve only first-time homebuyers or persons below median income, because the private sector can now serve the rest of FHA's market.

Each of these arguments is flawed. Let me discuss them briefly.

A. ELIMINATION OF FHA

Some argue that the private sector can now serve most of the need served by FHA and so FHA can be eliminated without any significant loss to the public interest. While the private sector should be commended for its continued innovation and efforts to serve more of the unmet need, the overlap between FHA's current borrowers and those served by the private sector is very small. Five reasons explain why:

1. FHA premiums are higher than PMI premiums, so FHA serves borrowers who cannot qualify for lower premium, privately-insured loans. Lenders will guide borrowers to the lowest cost alternative or risk loosing business to their competitors.

2. FHA's downpayment requirements remain far lower than conventional mortgages. In 1993, 62 percent of FHA borrowers paid less than 5 percent down, but less than one percent of comparable (below FHA loan limits) GSE-purchased loans had less than 5 percent down. Conventional 3 percent downpayment programs are reserved for borrowers who otherwise meet the more stringent PMI underwriting requirements. FHA, in contrast, allows downpayments smaller than 3 percent for mortgages of less than $50,000 and permits the 2.25 percent up-front premium to be financed.

3. FHA underwriting criteria allow many to use FHA who do not qualify for PMI. FHA does not require borrowers to maintain contingency reserves as private insurers do. Its qualifying ratios allow borrowers to use more of their income for debt and housing costs. FHA borrowers can use gifts from relatives to make their

downpayments. And, FHA is more tolerant of less-than-perfect credit histories so long as borrowers show a willingness and ability to pay.

4. FHA loans are disproportionately on smaller and older properties and in inner-city and other underserved areas. Twenty-eight percent of FHA mortgages in metropolitan areas benefitted underserved areas, while only 15 of conventional conforming loans were in these areas.

5. FHA offers 100 percent insurance, as opposed to the 30 percent insurance offered by the conventional market. If lenders perceive potential risk to them, perhaps associated with the age of the property or the area or regional economy, they will not makes many FHA-type loans in the absence of 100 percent insurance.

B. Privatization of FHA

This argument amounts to the elimination of FHA. FHA's ability to serve borrowers that the private sector cannot serve rests on its backing by the Federal Treasury and its freedom from having to earn profits for its shareholders. These advantages are lost if FHA is privatized. A private FHA will simply replicate the business that the existing private mortgage insurers provide today.

C. Targeting of FHA

This argument assumes that there is substantial overlap between the borrowers served by FHA and those served by the private insurers. In reality, the overlap is quite small. A large portion of those borrowers served by FHA whose incomes exceed median income do not qualify for privately insured mortgages, as discussed above. A recent study by The Secura Group found that over half of FHA borrowers were left with less than $2,000 in liquid assets after closing and an additional 20 percent were left with less than $3,000. Most of these borrowers would not meet the PMI's higher downpayment, closing cost, and reserve requirements.

In addition, FHA's strength comes in part from the diversity of its portfolio. The Secura study found that, to remain actuarially sound, a targeted FHA would need to increase significantly its premiums. Those higher prices would make home ownership unaffordable for many lower-income FHA borrowers. The result of targeting FHA would be lower home ownership rates, as both groups are left with no financing alternative.

V. Conclusion

Mr. Chairman, the new FHC, consolidation of insurance programs, greater flexibility, and enhanced oversight will allow the Federal Government to continue prudently to fill the gaps which others, with private profit motivation and higher costs of business, simply cannot meet. Our country is strong because it has one of the highest home ownership rates in the world. Community stability and pride is built on high home ownership rates and good quality housing. That is FHA's legacy, but the job is not done. You have the opportunity to create a streamlined, downsized, entrepreneurial public entity to complete this work, at no cost to the taxpayers. We look forward to working with you in shaping the future.

PREPARED STATEMENT OF STEPHEN MOORE

Director of Fiscal Policy Studies, CATO Institute, Washington, DC

May 4, 1995

Thank you Chairman Mack for the opportunity to testify on the mission of the Federal Housing Administration.

Let me state my conclusion at the start: FHA should be privatized, and if not privatized entirely, vastly scaled back. There are three major reasons why Congress should end taxpayer subsidies to FHA:

(1) *Today FHA almost entirely duplicates private industry.* The FHA's primary mission today is to compete with a vigorous and healthy private mortgage insurance market. As a general principle of good government, it should not be the role of Federal agencies to compete with private industry. FHA was created in the 1930's to fill a market void. That void no longer exists. Nearly half of the mortgage insurance market today is served by the PMI's—a percentage that is rising. At least 60 percent of FHA's business would be handled by PMI's except for taxpayer subsidies and liberalized lending practices at FHA.

(2) *FHA has strayed far from its original mandate of serving low-income, first-time homebuyers.* Increasingly, FHA does not serve low-income minority homebuyers. The FHA has aggressively moved into more upscale housing markets. Today, with its $153,000 mortgage cap—up from $67,500 in 1980—FHA is serving

wealthier families. These markets are already well-served by the PMI's. Only 18 percent of FHA loan applicants in 1993 were for homes in low- or moderate-income census tracts. Moreover, in recent years roughly 30 percent of FHA's business has been mortgage refinancings. In other words, almost one-third of its insurance does not even cover a new home purchase.

(3) *To compete with private insurers, FHA has been forced to take on riskier loans.* On a level playing field, FHA is increasingly incapable of outperforming the efficient PMI's and their wide-range of innovative underwriting services. To retain its market share FHA must resort to questionable underwriting practices that put the taxpayer and homebuyer at great risk. These include the 100 percent guarantee, the higher loan-to-income ratio, a capital reserve on its $348 billion contingent liability that is about one-third the private industry standard, and most importantly, downpayment requirements of as little as 2 and 3 percent.

In sum—and this is the key point—FHA can only compete in the modern mortgage insurance market by putting the taxpayer at ever greater risk of multibillion dollar losses.

Background

I first became involved in the FHA issue some 10 years ago when I worked at the Heritage Foundation. When I began investigating the underwriting practices at FHA, I became aghast at FHA's failure to take prudent measures to protect taxpayers from the very rapid increases in risk (its credit ceiling tripled from about $40 billion to $130 billion from 1980 to 1986) that it was taking on. The study I published in 1986 issued this warning about the FHA:

> FHA has become a ticking fiscal time bomb that may soon explode in the taxpayers' lap. The frightening aspect of this growth in FHA credit is that this agency is failing to take prudent measures to protect itself and the taxpayer against the huge contingent liability the agency carries. Should the economy slide into a deep recession, the FHA could easily be facing multibillion dollar losses.

The response to this study "How Congress Can Defuse the FHA Time Bomb" was remarkably incendiary. The mortgage bankers and realtors relentlessly vilified me and the study. They said that it was scare-mongering, irresponsible, and baseless hyperbole. They said that FHA was in stellar financial shape. In other words, their view was: Don't worry; be happy.

Then in 1987 the time bomb exploded. In 1988 the FHA lost a record $1.4 billion. Foreclosures on FHA properties in many States with especially severe real estate slumps more than doubled. Fortunately, one result of all this was that some of FHA's most irresponsible underwriting practices were ended with sensible reform legislation in 1990.

But the whole incident revealed to me the extent to which this agency has been completely captured by private industry interests. It was telling that not a single low-income advocacy group or any social service organization from minority communities uttered even a word of objection to the study. It was private housing industry groups, allegedly representing the interests of low-income homebuyers and minorities, who howled in protest.

This suggests who the prime beneficiaries of the FHA really are.

Do We Still Need An FHA?

The subject of this hearing is: What should be FHA's mission? To answer this, let's go back to the FHA's *original* mission—something the agency has wandered far from. For some 50 years the stated mandate of the FHA has been to complement, rather than supplant the private insurance market. This is how Congress stated the point back in 1948 with the passage of the National Housing Policy Act. "The policy to be followed in attaining the national housing objective hereby established shall be: (1) private enterprise shall be encouraged to serve as large a part of the total need as it can; (2) Government assistance shall be utilized where feasible to enable private enterprise to serve more of the total need.

If we still abided by that mandate then for all intents and purposes, there would be no FHA today. Increasingly, private insurers are becoming capable of serving *all* of "the total need."

Today the private sector provides low downpayment mortgages to borrowers who once would have only been served by FHA. Almost half of all mortgage insurance today is provided by the private sector. FHA now only serves 17 percent of the market and about half the insured mortgage market.

FHA has attempted to recapture market share by relaxing its underwriting standards. One of the most disturbing trends at FHA from the taxpayers' perspective is the decline in the standard downpayment on FHA loans. When FHA was first start-

ed its standard policy was to insure 20 year mortgages with 20 percent down- payments. Over the years FHA has continually liberalized these standards—especially in recent years. Even as recently as the mid 1970's the FHA normally required 10 percent downpayment. But from 1977 to 1985 FHA lowered its minimum downpayment requirement three times. And it's getting worse every year. According to the Department of Housing and Urban Development's own data, the loan to value ratio of FHA loans continues to climb:

Median FHA Loan To Value Ratio

1988	92.8 percent
1989	93.1 percent
1990	93.5 percent
1991	94.7 percent
1992	95.0 percent
1993	95.3 percent

Today the median FHA loan has a downpayment of less than 5 percent. Why should this be a concern? The answer is that the size of the downpayment is the single most important predictor of loan default. It is much more important than the income of the home purchaser, for example. According to David Maxwell, former chairman of the Federal National Mortgage Association, "The conclusion is inescapable that the most central element in weighing the soundness of a mortgage loan is the amount of the homeowner's equity."

The 1990 emergency reforms somewhat lowered the maximum loan-to-value ratio for an FHA insured home to 97.75 percent for homes over $50,000 and 98.75 percent for homes under $50,000. But these ratios are still well above the private industry average of 5 percent downpayment. Worse yet, because the homebuyer is permitted to finance the up-front-mortgage insurance premium, on many FHA insured-homes, the loan to value ratio approaches 100 percent. This creates a perverse incentive system whereby in many cases it is more attractive for a financially troubled family to walk away from the home, rather than to sell it.

Why do we tolerate such unsound underwriting practices in Government? The answer seems to be that the housing industry has come to dominate the FHA agenda. The FHA is a case study of a Federal program where the taxpayers' interest has been subjugated to the special interest. By resorting to liberalized loan insurance practices, the FHA hopes to out compete the private sector.

Does The FHA Promote Home Ownership?

The standard argument for preserving the FHA is that it serves low- and moderate-income homebuyers who would not otherwise be able to afford a home. This may have been true 10 years ago. Today, the argument is increasingly suspect. Here are several reasons why:

(1) *FHA increasingly does not serve low-income homeowners.* In 1993 only 18 percent of FHA insurance applicants were purchasing homes from low-income census tracts. About 16 percent of PMI loans were from these areas. Federal Reserve Bank economist Glenn Canner recently compared the PMI's with FHA with respect to serving low-income areas. He concluded: "The [private] insurance programs seem to have a similar distribution of applicants across neighborhoods grouped by income, but the FHA and VA generally serve a lower- income clientele.

Also of note: The PMI's were more likely to approve insurance for homes in low-income neighborhoods than FHA. PMI's approved 79 percent of such loans in 1993. FHA approved just 73 percent.

Some low-income areas seem to be virtually quarantined by FHA. For example, a recent study found that 94 percent of the mortgages in South Central Los Angeles were conventional mortgages, not FHA. Isn't South Central precisely the kind of neighborhood that FHA is expected to serve? FHA does not; the private sector does.

(2) *Low-income markets will be well served without FHA.* In 1993 the majority of applicants for private mortgage insurance had incomes that were below the median-family income for the metropolitan area. In fact the fastest growth area for private insurers is the affordable housing markets. According to a recent article in *Mortgage Banking*: "The private mortgage insurance industry—comprised of mortgage lenders and mortgage insurance companies working with Fannie Mae and Freddie Mac—have been focusing on the affordable housing market with increasing intensity since 1989, yielding numerous initiatives . . . Fannie Mae, for example, which set a goal of $10 billion of affordable loans delivered by 1994, has reached its goal." Here's just one example: In 1994 GEMICO insured $1.7 billion under the Community Home Buyer's program—which is targeted for low-income home purchasers.

The PMI's are also experimenting with 5 and even 3 percent downpayment loans to expand in low-income markets. (The 3 percent downpayment loans do not allow the financing of the premium, however, as FHA does.) Not surprisingly, even FHA's strongest allies acknowledge that at least 60 percent of FHA loans would be handled by the PMI's if the FHA were closed down.

(3) *FHA's underwriting practices actually harm low-income housing markets.* Congress should recognize that there is something much worse than turning a family down for a mortgage, and that is approving a mortgage that a family cannot afford to pay. There is nothing more disruptive to the life of a family than having to lose a home by foreclosing on the mortgage. FHA does no service by pushing families into homes they cannot afford to pay for. But FHA does this routinely through its unjustifiably low downpayment policy and its 100 percent coverage.

The latest FHA budget reveals that total foreclosures soared to 100,000 in 1994. Over the past 10 years more than 700,000 families suffered the trauma of losing their FHA-insured homes. These foreclosures cost taxpayers about $5 billion per year. In these cases, the families lost; the taxpayers lost; the neighborhoods lost; only the mortgage bankers won. And they aren't generally of low income.

One impact of FHA foreclosures is to destroy low-income neighborhoods—the very areas that FHA is said to be revitalizing. Gail Cincotta, the head of the National Training and Information Center in Chicago, and a long time slum-fighter, says: "The Number 1 problem in revitalizing neighborhoods is FHA." She notes that in many low-income neighborhoods, FHA's default rate is 28 percent. By contrast, private insurers will work with the financially distressed homeowner to refinance the mortgage and make other accommodations to keep the family in the home.

Privatize FHA

The Mortgage Bankers Association recently published a study suggesting that as many as 150,000 home buyers would be "shut out" of the housing market if FHA were cutback. What MBA did not say is that a great number of these 150,000 loans should never have been originated in the first place. They are unsound loans that have a high risk of default. Tightening FHA's underwriting guidelines to meet private sector standards, or closing down the FHA entirely, will not mean that these families cannot buy a home. It means that they will have to either buy a slightly less expensive home, rather than one they can't afford, or that they will have to delay a home purchase until they have more equity.

The purpose of Government is not to compete with private industry. This is precisely what FHA does today. It serves the same market as private insurers and stays in business only because of its unsound underwriting practices and its direct line of credit to the Federal treasury. This direct line of credit creates the illusion that FHA is "profitable." It is only profitable to the extent that it requires taxpayers to spend its $380 billion contingent liability—one that could once again detonate in the taxpayers' lap.

If FHA cannot be immediately privatized, then Congress should require that it follow the same underwriting standards of private industry. FHA should:

(1) Raise the minimum downpayment to 5 percent on all its insured-homes.

(2) End the 100 percent insurance coverage on FHA loans. This only encourages mortgage bankers to initiate questionable loans, because all the risk is borne by the taxpayer. FHA should only cover 30 percent of the losses on a foreclosed property. Even VA covers

(3) Prohibit borrowers from financing in the mortgage the insurance premium.

(4) End FHA refinancing.

(5) Lower the ceiling on FHA loans to homes of less than $100,000. The market above $100,000 is already well-served by the private sector. The cross-subsidy argument is spurious. It could be used to justify the FHA insuring $1 million homes. The FHA should be required to make sound loans for low-income homeowners by raising the downpayment threshold. Then, no cross-subsidy would be necessary.

(6) Require the FHA to move toward a 4 percent reserve fund on its liability—the private sector industry standard—to protect against taxpayer losses.

(7) Immediately close down the FHA multifamily program, which has experienced huge losses, and replace it with a low-income housing voucher program. We should use our affordable housing dollars to empower low-income residents, not mortgage bankers and developers.

PREPARED STATEMENT OF G. RICHARD DUNNELLS, Esq.

HOLLAND & KNIGHT, WASHINGTON, DC

MAY 4, 1995

Mr. Chairman and Members of the Subcommittee: Thank you for giving me this opportunity to share my views on the future role and structure of FHA. My name is Dick Dunnells. I'm a Washington, DC attorney, formerly with the law firm of Dunnells & Duvall and now with the law firm of Holland & Knight. I served 4 years at HUD between 1969 and 1973 under then HUD Secretery George Romney with primary responsibility for the post-construction, loan management side of FHA. I served on President Reagan's Commission on Housing during 1981 and 1982 and was a member of its Housing Programs Committee which studied and made recommendations on all HUD/FHA housing programs. As a private attorney, I've represented HUD/FHA as a client as well as representing private and public parties and agencies before HUD/FHA for the past 22 years.

It may not be fashionable to say, but I care about and have respect for HUD/FHA as an organization, as an institution, for its mission and for the objectives of its housing and community development programs. But I support the forces of change and innovation which are now sweeping HUD/FHA and I applaud those of you who work to achieve reasoned and considered change for HUD/FHA in the cost effectiveness and quality of its operations and programs. Putting aside individual debates and differences and the various political agenda which surround the subject of needed changes in HUD/FHA, in the 26 years that I've been involved with HUD/FHA I have never seen such unanimity on the basic proposition of the need for significant and structural change at HUD/FHA. There is a real "sea change" going on with respect to HUD/FHA. This is good. This provides an opportunity for real structural and programmatic improvement.

I'll limit my comments to basic, threshold issues:

- *Should FHA be reserved as a vehicle to effect national housing policy?*
- *If so, what are FHA's appropriate roles and missions?*
- *Should FHA be left in its present form, sold, and privatized, or restructured as a Government-owned corporation?*

I'll direct my comments to the multifamily residential and health care facility programs of FHA since those are the programs where I've had the most experience. And when I speak of FHA, I am speaking of FHA as a Federal mortgage insurance and credit enhancement agency whose basic mission is to promote the supply of private mortgage credit to construct and rehabilitate multifamily residential and health care facilities. I am not speaking of FHA as an agency which dispenses rental assistance subsidies to tenants or projects or acts as a provider of social welfare services to those in need. In my view, those are appropriate missions for other Federal, State, and local agencies. They are not appropriate missions and responsibilities for FHA.

Finally, when I speak of FHA, I include GNMA since, in my opinion, GNMA should be consolidated with FHA as it once was. It makes no sense to maintain a separate FHA and a separate GNMA.

Should FHA be preserved as a vehicle to effect national housing policy?

I feel somewhat at a loss when someone asks me to describe our "national housing policy." For me, the term "national housing policy" is something of a moving target and largely depends on who's doing the talking and when. We haven't had a clear-cut statement of "national housing policy" since the 1960's. Accordingly, it's easier for me to talk in terms of national interests and national needs.

We've got a society in which racial, economic, age, and ethnic polarization are escalating; where our cities and inner-city neighborhoods are in decline; where shortages of affordable rental housing for our lower-income families, elderly, and special needs persons are becoming more and more severe. Perhaps you've seen the recent report of the Low-Income Housing Information Service which found that over 27 million American families are either homeless, live in substandard housing or pay more than 30 percent of their incomes for housing because of the scarcity and high cost of unsubsidized rental housing. The amount of affordable multifamily housing development (new construction and rehabilitation) going on in America at the present time (and over recent years) is "peanuts"; and anyone who thinks that the private sector credit markets, State or local housing agencies, FNMA or FHLMC standing alone will meaningfully address and correct this situation is simply kidding himself.

When it comes to financing the development of health care facilities (hospitals, nursing homes, intermediate care, assisted living, board and care homes) particu-

larly in our central cities, it is extremely difficult to find private mortgage credit sources for refinancing and rehabilitating existing facilities or for the construction of new facilities on terms which make economic sense. Those health care conduit financing programs that you hear about are only interested in the "high-end" projects—the "cream".

Promoting the development of affordable family, elderly, and special needs multifamily rental housing and health care facilities where private sector, local or State agency or GSE mortgage credit sources cannot or will not respond is, in my opinion, a national interest and a national need to which FHA is uniquely equipped to respond. Simply stated, there is no private or public sector equivalent to FHA. FHA serves housing needs and housing markets which no other private or public sector mortgage credit sources have and (in my opinion) will adequately serve. Particularly with the continued thrust to uncouple project-based Section 8 rental subsidies from multifamily rental projects, FHA is needed to promote the supply of private sector mortgage credit for the construction and rehabilitation of affordable rental housing. Neither the private sector, FNMA, FHLMC or State and local housing agencies standing alone are going to meet this need without project-based subsidies—particularly in our central cities where the affordable housing needs of our minority, immigrant and special needs families and persons are the greatest. On the other hand, FHA can meet and has met this need. I recently saw some Mortgage Banking Association statistics that showed that:

- Fifty percent of residents of FHA-insured unsubsidized projects are families at 80 percent or less of median income; 82 percent of such residents are families at 100 percent or less of median income;
- Thirty-two percent of residents of FHA-insured unsubsidized projects are minorities; and
- Sixty-three percent of the multifamily unsubsidized mortgages insured by FHA are on projects located in central cities.

Then too there are the historic roles FHA has played in developing the capacity of local and State agencies to perform greater roles in the financing and development of affordable multifamily and special needs housing; in stabilizing the supply of mortgage credit in markets that have gone sour (remember the early 1990's when FHA was about the only multifamily finance game in town); in providing emergency housing resources in the face of national disasters; and in developing and standardizing new and innovative mortgage credit instruments and financing techniques. Last, but not least, FHA has acted as a national advocate, analyzer and demographer of housing interests and needs which cut across geographic, urban/rural or ethnic/racial boundaries. And FHA has been a principal support mechanism for the huge housing component of our national economy and gross national product. What entity or agency other than FHA can or should perform these roles?

Yes, I believe FHA should be preserved since today there are no equivalent public or private sector entities or agencies which can address and serve the above Federal interests and needs as well as FHA.

If FHA is to be preserved what are its appropriate roles and missions?

First and foremost, FHA's role should be that of a self-sustaining mortgage insurance and credit enhancement agency whose mission is to facilitate the supply of private sector mortgage credit to finance the development (new construction and rehabilitation) of affordable multifamily, elderly, and special needs housing and health care facilities in partnership with private sector, GSE, State and local entities and agencies. FHA should not be charged with the mission of providing and administering rental subsidy programs such as rent supplement or Section 8. Other agencies, Federal, State and local, are much better suited to perform this role of addressing the income needs of lower income, elderly and special needs renters.

When you look back over the 60-year history of FHA and the evolution of its multifamily programs, you see the 1960's as the turning point in FHA's basic mission when it was given the responsibility to serve lower-income persons who could not afford market-rate housing. The problems that arose thereafter were not from the public purpose of that assignment, but from the pattern that emerged of Congress repeatedly insisting that FHA do things which it was not designed and equipped to do. Then, when failures and problems occurred (and without assuming responsibility) for Congress to attack FHA, its employees and its programs; and then, when another special interest or crisis arose, turning right around and making the same type of demands upon FHA. And so it goes.

Many existing FHA multifamily programs should be consolidated, restructured, or scrapped. But FHA's capacity to underwrite and insure mortgages on a loan-by-loan basis should be preserved—particularly in the case of projects for lower-income fam-

ilies, elderly and special needs persons and projects which are part of inner-city revitalization efforts where private sector mortgage credit is unavailable.

In the case of FHA's health card facility programs (Section 242 for hospitals and Section 232 for nursing homes, assisted and intermediate care facilities, board and care homes), these programs have been successes and have served to attract private sector financing which would otherwise not be available. The Section 242 hospital program has insured over 280 projects with $7.4 billion in mortgages, has a claim rate of 2.7 percent and has generated approximately $242 million in net income to FHA. The Section 232 program has insured over 2,000 projects with $5.6 billion in mortgages and has an overall default rate of 8.6 percent which has dropped to under 4 percent in recent years. Importantly, in these times of debate over our national health care system and efforts to devise ways to reduce the cost of health care, FHA should continue to be an innovator in health care facility financing which can lower health care costs and Medicare contributions.

FHA should significantly expand its involvement in innovative new forms of multifamily credit enhancement techniques in partnership with FNMA, FHLMC, and State and local housing agencies. Some examples of such innovative forms of credit enhancement that are flexible and are designed to give FHA's private or public agency partners the opportunity to select those FHA credit enhancement products that best fit the proposed project or transaction with acceptable risk to FHA are:

- Risk sharing products where both FHA and the private or public sector partner shares in the risk of loss and FHA is involved in the initial approval of the partner, in providing an underwriting review and in monitoring servicing and asset management.
- Pool insurance where FHA would insure a pool of multisource mortgage loans originated by regional or national conduit partners.
- FHA first loss insurance where the top 5–10 percent of the insurance risk is taken by FHA.

FHA should renew its historic role as an innovator of forms of mortgage credit instruments and should be a vehicle far disseminating new techniques and strategies for financing and developing affordable and special needs housing.

Last, but certainly not least, FHA must continue to support and protect the huge Federal investment that exists in FHA's portfolio of insured and HUD-held multifamily residential and health care facility mortgages. FHA has an inventory of approximately 14,500 multifamily projects with approximately $47 billion in FHA full insurance and co-insurance in force; 937 health care projects with approximately $8.0 billion in FHA full insurance and co-insurance in force; an FHA-held multifamily mortgage portfolio of approximately $7.5 billion covering some 2,250 projects; and approximately 5,004 Section 202 direct loan elderly and handicapped projects with total mortgages of approximately $10.2 billion. Clearly a major role for FHA is the preservation of this portfolio of properties and mortgages and the disposition or restructuring of those subsidized multifamily properties and their mortgages as current project-based Section 8 subsidy programs are changed or eliminated and as the properties themselves continue to age without adequate physical improvement reserves.

Should FHA be left in its present form, sold and privatized or restructured as a Government-owned corporation?

Although the costs, complexities, and dislocations associated with the privatization or restructuring of FHA to a Government-owned corporation should not be minimized, FHA should not be left in its present form with a commitment to simply improve the delivery system. FHA's programs have become over regulated, too complicated and are administered with slavish commitment to process and not to product. The intertwining of project-based subsidy programs and FHA mortgage insurance programs has become too embedded to be unraveled. The array of FHA programs itself, with some programs virtually unused, some targeted to small and parochial interests, and some nothing more than vestiges of programs which have been on the books too long, underscore the lack of a focused, considered and effective program mission strategy for FHA. Within the organization itself, there is a lack of professionalism, a lack of discipline and even a lack of respect for and loyalty to the organization itself. The most virulent criticism of FHA that I encounter comes from within FHA itself. In short, the malaise and the problem goes much deeper than simply a lack of staff or staff training.

I say this without criticism of people at FHA such as Nic Retsinas who heads FHA, Helen Dunlap who heads FHA Multifamily, Linda Cheatham who heads FHA Multifamily Development and Albert Sullivan who heads FHA Multifamily Loan Management. These and others are bright, energetic and committed people who are

doing their best to improve FHA's programs and delivery system while working within a dysfunctional FHA organization and against existing bureaucratic and regulatory constraints which defeat the best of initiatives.

I do not see the privatization of FHA's multifamily and health care programs as a desired or viable option. First, these FHA programs are not, for the most part, in competition with private sector mortgage insurers or with FNMA or FHLMC. Second, only as a Government-owned and controlled agency can FHA serve the national interests and needs which I've discussed earlier. Third, a Government-owned and controlled FHA is needed to protect the enormous national investment and interest in the existing FHA portfolio of multifamily, elderly, and special needs residential housing and health care facilities.

Why privatize FHA's multifamily programs operations when there is an option and an opportunity on the table to return FHA to a self-sustaining, professional and effective delivery vehicle for mortgage insurance and credit enhancement to private and public sector entities and agencies, and to serve those national interests described above? I would pursue restructuring FHA as a new Government-owned and controlled corporation along the lines proposed by Secretary Cisneros and Assistant Secretary Retsinas. I've read the draft charter for the new Federal Housing Corporation and it generally makes sense to me; although I would hope that in the structuring of the Corporation staff resources would not be dissipated by replicating the 80-plus HUD field office configuration. I'd consolidate and regionalize the Corporation's offices and staff to maximize professional capability, and underwriting and monitoring disciplines.

In the case of FHA's single-family mortgage insurance programs, I don't have the quite the same views on role and mission that I do for FHA multifamily programs. In FHA single-family programs, the areas of overlap between FHA and private sector mortgage credit sources are much greater, both in the primary and secondary mortgage markets. There is no question but that FHA's single-family mortgage insurance programs have been a huge success over their 60-year history and have served, and continue to serve, large segments of our society who do not have access to affordable home purchase mortgage credit, *i.e.*, first-time homebuyers, lower-income and minority home purchasers, etc. Moreover, FHA single-family programs continue to provide stability to the supply of mortgage credit in many markets and provides an enormous informational resource regarding housing and home ownership demographics and statistics.

But, I don't feel qualified to comment on the proposal of the private mortgage insurers (PMI's) to limit FHA single-family programs to first-time homebuyers and low-income home purchasers. The PMI's talk a good game but I'm not satisfied they can replace FHA single-family programs as a stable and reliable national source of mortgage credit. We've seen the flights of the PMI's when housing markets head south, risks increase and profit margins decrease. My initial reaction to PMI's targeting proposals for FHA is that it sounds like a bad idea which will relegate FHA single-family programs to being a low-income, subsidized housing agency with increased risk, cost and failure rates.

In short, I believe that FHA single-family mortgage insurance programs should be continued but only with clear and unequivocal direction that FHA single-family's role be shifted over time from that of a mortgage insurer to that of a pool insurer, coinsurer or reinsurer. In other words, that FHA move out of the "retail" segment of the single-family mortgage market.

That being said, let me return to FHA multifamily and health care facility programs to conclude. In my view, FHA continues to serve vital national interests and needs and should not be abolished. It should become a Government-owned and controlled corporation with authority to provide innovative credit enhancement to promote the flow of private mortgage capital to serve low- and moderate-income families, elderly and special needs persons and needed health care facilities. Providing subsidies, whether project-based or tenant-based, should not be part of FHA's mission.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MACK FROM NICOLAS P. RETSINAS

FHA's insurance program does not exclude home buyers who qualify for private mortgage insurance from obtaining FHA insurance.

Q.1.a. Is it true that some of FHA's single-family insurance business is generated by home buyers who could have obtained private mortgage insurance on their loans?

A.1.a. Few FHA borrowers could have obtained private mortgage insurance on the loans that FHA insured. If privately insured loans were available to FHA borrowers, they would have taken advantage of them, as private mortgage insurance is less expensive than FHA insurance. To the extent that lenders influence whether home buyers use either private or FHA mortgage insurance, most lenders have a competitive incentive to send customers to the lowest priced product, if they qualify.

FHA insures primarily loans that would not qualify for private mortgage insurance. Even when the downpayment is large enough to meet PMI requirements, most FHA borrowers need one or more of the other aspects of FHA underwriting that are more flexible than PMI's. For example, FHA allows borrowers to use a greater proportion of their income for debt and housing costs; FHA allows borrowers to finance closing costs; FHA allows borrowers to use gift letters for all of the downpayment and closing costs; FHA does not require borrowers to have 2 months mortgage payments held in reserve; and FHA is more tolerant of minor credit blemishes. The new, pilot, low downpayment programs offered by the PMI's are not available to borrowers who need these other aspects of FHA underwriting to qualify.

Q.1.b. If so, to what extent is FHA's single-family mortgage insurance cutting into private mortgage insurance business? Also, to what extent is FHA serving only underserved markets whose ownership needs are not being met by the private sector?

A.1.b. Very little. As noted above, most FHA-insured loans would not have qualified for private mortgage insurance. FHA does not have an exclusive franchise on any borrowers. PMI's, with a less expensive product, should be able to compete away any incidental business that goes to FHA but would qualify for PMI.

During good economic times, FHA's market share drops significantly, as low-interest rates and high growth allow more home buyers to qualify for privately insured loans. However, when economic conditions decline, PMI's cannot profitably insure as many borrowers and their criteria exclude more of the market; at these times, FHA's market share grows. The important point is that capital continues to flow to housing, preserving home ownership opportunities and homeowners' equity in their homes. When it can, the private sector serves more of the need; when it cannot, the Government is available to fill the gap. And because of the Government's lower cost of capital, it can do this without costing the taxpayers a dime.

Q.2. Obviously, lenders are not required to offer FHA insurance, and many FHA lenders—mortgage bankers—are not covered under CRA. FHA cannot meet it's public purpose goals without the par-

ticipation and cooperation of the lending community. How do you propose to ensure that lenders fully participate in the FHA program?

A.2. We cannot compel lenders to participate in FHA but we can make participation in FHA lending desirable if we: (1) develop products that help lenders to meet the needs of their communities; and (2) make FHA more customer friendly, so that FHA lending is no more burdensome than other programs. We are making significant strides in both regards.

For example, in March of 1994 changes to the 203(k) program made it more user friendly. Various design restrictions were loosened, appraisal requirements were reduced, approvals were streamlined, and the eligible uses of funds for rehabilitation were expanded. Because the product was improved and because the process was simplified (and training to users provided), the number of lenders using section 203(k) increased by 500 since 1993 and HUD will increase production volume to about 8,000 units in 1995. HUD has seen an increase in both the number of lenders using the program and the number of nonprofit entities involved. There is no comparable vehicle for providing favorable financing for the rehabilitation of urban properties.

As another example, HUD has updated the technical capacity of the FHA to do business. This removes a reason for not doing business with the Government—that is, that it simply takes too long. HUD's Denver processing center has reduced the processing time for endorsing single-family loans from 2 to 3 months to an average of 2 days. In addition, electronic processing has reduced the amount of time to process a lender's claim to 1 day (from 5) and has reduced the processing time for a mortgagor's refund of the unearned premium charge to 30 days from 90.

HUD's legislative proposal for FHC would allow us to do far more to make FHA products desirable and thus help us to enlist lenders to reach underserved borrowers. Specifically, we'd have the flexibility to design new products to meet unmet needs. Moreover, we would be able to modernize far more quickly, without bureaucratic entanglements. Finally, our risk-sharing products would allow us to tap markets served by lenders who shied away from FHA but were willing to deal with our partners' more efficient delivery systems.

Q.3. You have identified the decline in home ownership rates, and the demographics of the population in which the greatest decline has occurred. To what extent is this decline the result of "lifestyle" factors, and how much is due to facts that can be corrected by changing FHA? Put another way, what do you estimate the universe of people to be who are going without a mortgage simply because they cannot get financing?

A.3. HUD cannot attribute a specific percentage of the decline in home ownership rates to lifestyle changes, although it is recognized that they have a significant role. The Joint Center for Housing Studies acknowledges that lower "headship rates, along with the shrinking population of 25–34 year olds, mean that the number of households in this age group is set to decline." In addition, "Trends toward delayed marriage and childbearing . . . have slowed the

growth percent of married couple households." Nevertheless, the Center states that "despite a general decline in costs, many low- and moderate-income households are still unable to move up the housing ladder to home ownership. For some households, the obstacle is lack of funds for making a downpayment on a home; for others, it is lack of housing suitable for purchase. And for still others, discrimination is the primary barrier to home ownership."

FHA will be an important partner in a National effort to address these needs. HUD's Home Ownership Strategy calls for specific actions from FHA and its public and private partners to:

- reduce closing costs;
- reduce paperwork and shorten the lending process;
- ensure the production of "starter homes" and the financing of rehabilitation for older existing homes;
- expand counseling for first-time home buyers;
- expand consumer awareness of the home ownership market.

Q.4. GAO reported in 1989 that HUD is but one of 16 Federal agencies that administer programs supporting public-private partnerships. GAO also testified at your forum last November that many people providing low-income housing were neither familiar with nor interested in HUD's FHA programs. Can other organizations within or outside the Federal Government, more efficiently and economically meet the needs of low- and moderate-income families for decent, affordable housing? Do they need traditional mortgage insurance programs offered by FHA to do it?

A.4. No other entity has the ability to provide Federal credit enhancement for housing. The backing of the U.S. Treasury produces the best credit in the world and therefore provides the lowest cost credit enhancement available. It costs the private sector significantly more to provide the exact same credit enhancement or insurance that FHA can provide because the private sector must set aside larger capital reserves and produce a greater return on equity for their investors. As a result, business that FHA can do on a self-sustaining basis, cannot be done profitably by the private sector.

With this powerful credit enhancement tool, other dollars can go further. Credit enhancement alone cannot make housing affordable to those who need subsidies, but it can leverage private investment and stretch scarce housing subsidy dollars received through HOME, low-income tax credits, or other sources.

FHA has not always used its credit enhancement as well as it could. At the forums, we heard again and again that FHA's multifamily insurance products were either irrelevant to the work of low-income housing providers or so difficult to use and time consuming to obtain that these providers did not even try. However, they also talked about the need for a flexible credit enhancement product that could work with the multiple layers of financing that affordable housing requires and that would help to gain access to secondary market sources of capital for the lenders who were making these loans. Our proposal for the new FHC would give us the flexibility to design new multifamily credit enhancement tools to meet these needs and new ones as market needs change.

In fact, FHA Multifamily programs already have changed to make them more efficient and relevant to the market. The FHA now operates risk sharing programs with the GSE's and State and local housing finance agencies. This makes best use of private sector expertise and encourages risk sharing between competent and well capitalized partners. FHA is analyzing its delivery system, loan terms, and underwriting in order to reduce risk and cost to the taxpayer with the objective of operating on a self-sustaining basis in the future. One key will be to underwrite the real estate and not the subsidy. In fact, the new corporation will not administer any subsidies.

Currently, 60 percent of the residents of unsubsidized, insured, rental housing are low-income—a strong record. About 37 percent of residents are minorities and about 63 percent of the properties are located in central cities. A recent study by Abt Associates on multifamily housing anticipates an improving financial trend in unassisted multifamily housing. This will be FHA's basic program emphasis going forward, and it should be noted that the recent audit of FHA reduced the multifamily loss reserve requirement due to an improved ability to recover more from claims and collect more in premiums.

Q.5. Under the restructuring, the public/social purpose of FHA would be retained. Obviously, this will mean that FHA will be operated in a *more businesslike*—not a *completely businesslike,* manner. There is no exact parallel between what the private sector does and what a Government corporation with a social purpose would do. Hopefully, the corporate structure is not being presented as a panacea for all the bureaucratic barriers FHA now faces. Would you care to comment about what our reasonable expectations should be about what this change will mean?

A.5. A private sector business is motivated by profit. The new FHC would be driven by two sets of performance measures: achievement of public purposes and safety and soundness. In exchange for this unprecedented level of accountability for outcomes, FHC must be freed from many existing bureaucratic barriers. Creation of a Government corporation is no panacea; however, in 1948, Congress recognized that certain governmental functions of a business-like natures were better performed in the corporate form, in which oversight would focus on results not process. Recreating FHA as a corporation will give FHC employees a distinct sense of identity and a better focus on achieving the bottom line (in this case the performance goals). Finally, the corporate form will serve as a reminder to others in the government (HUD, OMB, and elsewhere) that micromanagement is counterproductive.

A corporate form would be, however, only the first step in the transformation of today's FHA into a more entrepreneurial entity. Management would need to design incentives for employees that encouraged innovation and greater achievement of performance goals. New technology and business process redesign would need to be aggressively pursued. FHA is doing these things today, to the extent it is able under existing constraints. A corporate form would make this transformation easier, but would not ensure its success.

Only a commitment from HUD, the Administration, and the Congress could do that.

If successful, however, it would be reasonable to expect that a new FHC could make a valuable Government resource—its credit enhancement—go further, by serving more unmet housing needs, creating more homeowners, and serving the capital needs of affordable housing providers. It would do so with many fewer employees than it uses today. And it would provide the taxpayer with far greater assurance that it was protected from unexpected losses.

Q.6. It appears that this proposal would effectively merge the insurance funds. Is that true? If so, we would be taking the MMI Fund, which is inherently stable, and mixing it with Funds that are not self-sustaining? Does that not raise safety and soundness concerns?

A.6. HUD does not propose to merge the existing funds. The existing funds would remain intact in their current form to finance business done under the National Housing Act authorities. HUD does propose to create one or more new funds to operate its new business under FHC's charter authorities. Those lines of business, which would include single-family, multifamily, and health care, would be subject to a requirement that they were overall self-sustaining, requiring no appropriated subsidy. Each year, before any business were undertaken under the Charter authority, the safety and soundness regulator would be required to make a determination that the self-sustaining nature of the business as a whole would not be threatened by the proposed activities; and, each year, the safety and soundness regulator would review the outstanding business to ensure that there was no threat to capital adequacy.

We have not indicated which business lines would be operated out of which new insurance funds. That is a matter which would be determined in the business plans submitted to the Secretary and the safety and soundness regulator each year. There may be good reasons for segregating some business lines from others. For example, while self-supporting, the health care business is subject to certain risks uniquely in the control of government. FHC may think it prudent to segregate these risks from other business lines. However, those are judgments best made when the specific business lines—and associated risks—have been identified.

Q.7. I understand that greater procurement autonomy and better staffing resources would enable HUD to develop modern systems and processes comparable to the private sector. But the process of getting there from here is what troubles me. Can you comment generally on my concern that making this transition to the corporate structure will be worth the time and the financial and human resources it will take—*and that in the end FHA will be able to meet its mission more cost-effectively?*

A.7. You are right to be concerned that transforming today's FHA into an entrepreneurial and effective FHC will be a difficult and time-consuming effort. We have begun to make strides toward this transformation today both as a downpayment on the greater changes yet to come and to demonstrate that this institution is capable of strong management and meaningful change designed to

allow it to meet its mission more cost-effectively. For example, the 1994 Audit of FHA shows that:

- The Mutual Mortgage Insurance Fund is stronger than ever, with a capital ratio of 1.99 percent.
- The multifamily loss reserve for the General Insurance Fund has been lowered for the second year in a row.
- Both the single-family and the multifamily inventories have been dropping, resulting in lower losses and less of a negative impact upon communities.
- Processing has been streamlined in important ways, including the introduction of underwriting changes which make it easier to reach out to creditworthy, nontraditional, and underserved buyers.
- The Department has been able to use updated methods for asset management and has reduced the cost of claims through asset sales.
- FHA received a "clean" financial opinion.
- FHA has been streamlined through management changes to the field offices. The reorganization along functional lines has led to more responsive decisionmaking.

The new corporate structure will accelerate these beneficial changes.

Q.8. Under the new structure, to what extent will FHA's staffing and budget be dictated by OMB?

A.8. The FHC charter act provides that the maximum ceiling on FHC employees would be established by the Secretary and the FHC employees would count toward the HUD FTE cap. The cost of salaries and expenses are really part of the cost of providing credit. However, under Credit Reform, these must be budgeted separately. As FHC would be generating the funds to support its own salaries and expenses, there would be less incentive for OMB to micromanage these dollars but the opportunity would exist.

The budget system under the FHC charter act was developed, to the extent possible, to ensure that business concerns drive FHC's budget. The budget submission of FHC would contain aggregate estimates of credit subsidy (overall positive) for purposes of Credit Reform. These estimates, however, would be developed using the expectations of performance of FHC's business lines developed by the Safety and Soundness regulator in its review of the business plan. HUD's goal was to ensure that FHC was not subject to two separate regimes—safety and soundness and credit reform—each with separate rules. Thus, the regulator's estimates would be used for FHC's budget submission and OMB would accept these estimates unless it had reason to doubt their accuracy.

Q.9. The Office of Housing administers other functions besides FHA. These include the Real Estate Settlement Procedures Act, the Manufactured Home Construction and Safety Standards, and affordable housing goals for the GSE's. Who would perform these functions were the FHA insurance function to be split off?

A.9. These regulatory functions, like some of the grantmaking functions also performed by the Office of Housing, would be managed by the Department.

Q.10. In FHA's role as corporate asset manager under the proposed restructuring plan, there will undoubtedly be a focus on maximizing the return on the sale of Secretary-owned single-family properties. What impact will this have on home ownership programs, such as the HOPE 2 and HOPE 3 Programs or Single Family Demonstration Program, which utilize FHA properties to provide home ownership opportunities to low-income families?

A.10. HUD's reinvention blueprint terminates the HOPE 2 (a multifamily program) and 3 programs, the functions of which will be assumed by the Affordable Housing Fund. However, this program consolidation will not impede the FHA's ability to provide innovative methods for attaining home ownership.

The ability of the FHA to sell owned properties to State and local governments and to nonprofit entities will continue under both the single-family and the multifamily property disposition programs. HUD has had good success with the single-family property disposition initiative implemented in September of 1994 and has involved a wider variety of participants into its sales programs. The authority to do this, and to reap the advantages of both quick sales and wider buyer participation, will continue under FHC.

Similarly, HUD's reinvention initiative revamps the multifamily property disposition program to attain budget savings. However, the specific authority to sell properties to interested State and local governments and to facilitate sales of properties to nonprofit entities, including nonprofit resident management associations, is retained and will be used where advantageous. Previous restrictions upon project use were proposed to be removed.

In addition to preserving adequate authority to sell HUD-owned units for home ownership purposes, HUD will subject the new FHC to performance measures which demand home ownership results. Meeting such goals through property disposition activities as well as loan origination activities will be discussed with the FHC safety and soundness regulator.

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